Citizens Advice Scotland
Scottish Association of Citizens Advice Bureaux

Irresponsible Lending

A Consultation Response to the OFT

By Keith Dryburgh, Policy and Public Affairs Co-ordinator

Citizens Advice Scotland and its 71 CAB offices form Scotland's largest independent advice network. CAB advice services are delivered through 199 service points throughout Scotland, from the islands to city centres.

The CAB service aims:

to ensure that individuals do not suffer through lack of knowledge of their rights and responsibilities, or of the services available to them, or through an inability to express their need effectively

and equally

to exercise a responsible influence on the development of social policies and services, both locally and nationally.

The CAB service is independent and provides free, confidential and impartial advice to everybody regardless of race, sex, disability or sexuality.

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The Scottish Association of Citizens Advice Bureaux - Citizens Advice Scotland
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Introduction

1. Citizens Advice Scotland (CAS) is the umbrella organisation for Scotland's network of 71 Citizens Advice Bureau (CAB) offices. These bureaux deliver frontline advice services throughout nearly 200 service points across the country, from the city centres of Glasgow and Edinburgh to the Highlands, Islands and rural Borders communities.

2. CAS welcomes the opportunity to respond to the Office of Fair Trading's (OFT) consultation paper on Irresponsible Lending. Scottish citizens advice bureaux report cases on all aspects of consumer lending, and it is an important area of concern for clients in the current economic set of circumstances.

3. In 2006/07, 91,475 new debt issues were brought to Scottish bureaux – an increase of 4% on the previous year. This represents more than 250 debt issues brought to Scottish bureaux each day of the year. Consumer debt remains by far the most common single issue that clients bring to bureaux each year.

4. The explosion of credit, both in terms of type and amount, was a defining aspect of UK society in the late 90's and the early part of this century. While the credit bonanza has started to grind to a halt in the last year, the policies and practices that characterised this period are still the same. It is these policies and practices that are being so widely blamed for the financial crisis facing the banks and for the record levels of personal debt in the UK.

5. They have also had a significant impact on the individual citizen. The demand on bureau rises each year, placing strain on the money advisers. Much of this debt stems from irresponsible lending to individuals who could ill-afford to hold credit, and from unsympathetic and unhelpful attitudes to debtors who default.

6. This consultation response will outline the problems that bureau clients face with irresponsible lending, showing that creditors can be irresponsible at each stage of the credit cycle, from advertising to handling defaults. We argue that this evidence shows that the OFT's definition of irresponsible lending needs to be as wide ranging as possible to include all aspects of consumer credit lending.

7. The consultation response examines:

- Advertising and marketing
- Selling techniques
- Appropriateness of product to borrower
- Sale of associated products
- Account management (including handling of default/arrears)

Advertising and Marketing

8. Scottish Citizens Advice Bureaux have reported a number of clients who have been misled by advertising and marketing by a creditor. This is especially the case with daytime television advertisements which can be misleading with their claims of what the loan can do for the client.
9. In some cases, clients are required to pay a large fee upfront before they are offered credit after seeing an advert on television. Once this payment is paid, the client can find out that the advert was misleading in its claims.

An East of Scotland CAB reports of a client who responded to a misleading advert offering a guaranteed loan of £10,000. The client, who was unemployed with mental health problems, paid a fee of £49.95 in order to receive an offer of a loan. However, the client was made a loan offer of £3,000 with an APR of 45%. The client consulted the bureau as he had not been offered the guaranteed loan. The bureau wrote to the company stating that their loan adverts were misleading and that it should have been obvious from the loan application that the client would not qualify for a loan as high as £10,000. The fee of £49.95 represented a substantial part of his income. The company said that they were a loan finding service with the actual offers always being made by third party lenders – they refunded the client his fee. The bureau felt the case represents irresponsible marketing targeted at poor and vulnerable people.

10. Advertising through television and then agreement by telephone often leaves the client with little notion of the terms and agreements of a loan. The only chance a client may get to see the terms before making a commitment can be the small print during the TV advert. Clients are more likely to be impressed by the claims in the advert than they are to seek out the fine print. The result of taking these loans can be serious debt problems for clients.

A South of Scotland CAB reports of a client who took out a loan of £25,100 from a finance company having seen their TV advertisement. The client was impressed with the advert's claims that the loan would be fair and easy to process. The bureau found that the repayments will be £294.51 per month over a period of 300 months. The actual sum to be repaid on the £25,100 loan is £88,353.

An East of Scotland CAB reports of a client couple who had secured borrowing worth more than eight times their income after applying for a secured loan that was advertised on television. The clients recently bought a new-build home, with a mortgage of £256,000 and a secured loan of £46,000 for the deposit. The secured loan is up to date, but the mortgage is £4,500 in arrears, and it is now likely that the house will be repossessed.

Selling techniques

11. Scottish bureau advisers often find that clients lack knowledge of financial terms and conditions, and that this can prove particularly harmful when dealing with salesmen. Low income consumers tend to base decisions on weekly affordability, and often have little idea of the APR, length of agreement, and total amount due, of the credit they take out. This lack of knowledge, coupled with sales techniques can lead to one sided credit agreements.

> A North of Scotland CAB reports of a client who was misleadingly told that he was getting a discount from a cold call salesman. The client signed an agreement to have his fibreglass roof repaired and a conservatory built for a cost of £42,000. The salesman said that if he signed today, the sum would be reduced to £37,000. The bureau looked at the contract and found that the client will have to repay £70,000 over the next 10 years. The client is 65 and still has no details of the work that the company are planning to undertake.

12. It isn't just a client's lack of knowledge that can lead to a poor credit agreement, but can also be the active efforts of some salespeople to get the client to take out as high an amount of credit as possible. Bureaux have reported instances where a salesperson has mislead a client deliberately.

> An East of Scotland CAB reports of a client who purchased a new kitchen priced at £11,000 three years previously. At the time, she had wanted to pay outright, but the salesman had refused and insisted that she had to enter into a Hire Purchase agreement. The agreement made was for a ten year period for a total amount of £25,610. The client did not have a full understanding of this, thinking that the monthly repayments ran for only three years. The client wants to clear the debt, but the company are asking for a further £10,913 – the original cost of the kitchen.
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> A West of Scotland CAB reports of a client who signed an agreement for double glazing and agreed that the salesman could complete it. The client had clearly indicated that he did not want the optional payment protection insurance, but the salesman ticked the box on the agreement. The client signed the agreement for a total of £1,800, but the premium due on the insurance has increased the amount owed to £2,259.

13. As well as being misleading, salespeople can also be intimidating. This is especially the case for older clients living on their own who can struggle to say no once a salesman is in their home. In some cases, clients sign an agreement only to get a salesman to leave their house.

An East of Scotland CAB reports of an elderly client who was cold called by a double glazing firm and agreed for a salesman to call. After two and a half hours, the client signed an agreement which was non-cancellable. The client said that he only signed the agreement to get the salesman out of the house.

14. The act of cold calling can be an intimidating practice for clients, especially if this takes place on a client's doorstep. This practice also encourages clients to be tempted to take out unplanned and often unnecessary credit if it is offered in front of them and is portrayed as being a good deal.

Appropriateness of product to borrower

15. A hugely significant problem for Scottish bureau clients in recent years has been the inappropriate lending of credit to borrowers. The era of easy credit that has taken place over the last decade or so has led to substantial lending to clients who haven't been in the position to repay their debt. Bureau have seen numerous examples of clients being given substantial credit when they are unemployed, on a low income, suffer from mental illness, or are likely to be too old to repay the debt.

Low Income Clients

16. Scottish bureau debt clients are less likely to be in full-time employment, significantly more likely to be unemployed, and more likely to live in local authority housing, than the Scottish population in general. Bureau clients are therefore predominantly low income clients – and yet bureaux see cases every day of clients struggling with significant credit commitments.

17. There are few adults in the UK who don't currently have or have held credit. It isn't just consumerism that drives the demand for personal credit; it is also the need for credit to have enough income to live. Many low income consumers supplement their income with credit just to get by, or need credit to replace essential items, such as cookers, that they cannot afford on their income.

18. The credit market isn't working for low income consumers. Low income clients who need credit are often able to access it, but not at affordable levels. It is a feature of the financial services market that the cost of a small loan is disproportionately bigger than that of a large loan. The cost of credit is therefore greatest for those who need to borrow the least. It also creates a perverse incentive for banks to lend more money to customers than they need to in order to maximise income. The result is that low income clients often have access only to unaffordable credit, and, rather than dissuading clients from taking credit that they cannot afford, banks and others are encouraging these agreements. This can often lead to intractable debt problems for clients.

19. Scottish bureau have reported cases in which clients have been given credit that is highly disproportionate to their low level of income. In such cases, it is very difficult for clients to make repayments on a loan and consequently take out further credit to meet payments. This is an unsustainable situation for a client and leads to a circle of debt that is difficult to escape.

A West of Scotland CAB reports of a retired client who was given a loan of £30,000 by his bank. The client is a council tenant who lives on a pension of £900 per month. The client made repayments using five credit cards, but has now reached the limit on all of them. The client's total debt is now £47,000.

An East of Scotland CAB reports of a client who was offered a loan by her bank as she withdrew money from her account, despite having no disposable income and relying solely on benefits. The client went into her local branch to withdraw the last £6 from her account, and was offered a loan and a credit card by the bank teller. The client agreed, and received a £2000 loan and a credit card with a limit of £1500. However, the client only has a little over £4 a week in disposable income, and could never have been able to afford the offered loan. The client now has debts amounting to £4,785 with her bank.

An East of Scotland CAB reports of a client on income support who was given a loan of £10,000 from her bank. The client had approached the bank for a loan advising them that her income consisted of income support and occasionally £40 cash in hand weekly employment. The bank did not ask for proof of the client's income. The client already had debts of over £14,000 prior to asking for the loan. The client used the loan to supplement her income, and could only make the first few repayments. The client is a homeowner and is now forced into selling her home to repay this debt.

20. The argument behind lending to low income clients is the provision of a service to customers who otherwise would not be able to obtain credit. However, for many of these clients, credit does not answer the problems of low income, and merely exacerbates their problems to the extent that their low wages or benefits are completely swallowed up by their ever increasing debt.

21. Either creditors who make these provisions are unaware of a client's income (and are therefore not carrying out required checks), or are offering credit that they know that the client cannot afford. Either way, this type of lending is fundamentally irresponsible. This includes offering substantial credit to a client whose only income is from benefits or pensions, or who is unable to work due to a disability.

22. Credit cards are a significant source of debt for clients, and evidence from bureaux shows that it is very easy for clients with low incomes to obtain a credit card with a high credit limit. The On the Cards report, based on research with Scottish bureau clients in 2004, found that 55% of bureau debt clients have a credit card debt, with 14% of clients having at least five credit card debts.[1]

23. Credit cards often act to supplement a client's income in the short-term. However, as the client begins to reach the limits they become a source of long-term debt that a low income client cannot hope to repay.

[1] On the Cards research report - http://www.cas.org.uk/FileAccess.aspx?id=268

An East of Scotland CAB reports of a client without employment who has £23,000 worth of credit card debt. The client has four children and has not had paid work for many years. He has reached the credit limit on seven credit cards, none of which he found difficult to obtain. His creditors do not appear to have made any checks before providing cards and setting credit limits.

A West of Scotland CAB reports of a young student, living with his partner and one dependent young child, who managed to run up nearly £10,000 of debt on six credit cards. Given the circumstances of the client and his partner, the bureau questioned how the client had been able to open six credit card accounts. The client reported that a finance company was willing to offer a consolidation loan despite the client having no disposable income to service the loan.

Clients with health problems

24. Our evidence shows that credit is being given irresponsibly to clients who do not work due to health problems, and are in receipt of out of work benefits. Creditors appear to provide these clients with substantial amounts of credit, despite benefits being their only source of income. This is not to say that this group of clients do not need credit. However, this credit is often provided at a level that is highly inappropriate for the client.

25. CAS published a report in 2006[2] on the costs of illness and disability on CAB clients. The research found that clients in the survey were more than five times as likely as the general population to be in financial difficulty. More than half (57%) had outstanding debts or arrears, with credit card debt being the most common (45%). Irresponsible lending to this group has a significant impact on clients who are far more likely than the general population to have financial difficulties and who are unlikely to have significant disposable income.

A North of Scotland CAB reports of a disabled client who has been unable to work for over a decade yet was given a £10,000 loan from his bank. The client's income consists of Incapacity Benefit, Disability Living Allowance, and war pension, amounting to £160 a week. The client tried to negotiate lower payments but the bank refused and would only accept the agreement amount. The client has now fallen behind on his payments, which is causing the client considerable stress.

An East of Scotland CAB reports of a client who has built up a debt of £75,000 mostly on credit cards despite being in receipt of incapacity benefit for many years. The client has 18 debts, most of which are credit cards. The client's creditors were aware that the client had no income other than incapacity benefit, yet still provided loans and credit cards.

A West of Scotland CAB reports of a client whose bank has lent him substantial sums of money despite his only income being Income Support and Disability Living Allowance. The client has now received over £10,000 of loans from his bank. The bureau wrote to the bank querying why a client whose sole income was benefit payments was given such substantial credit, but did not receive a reply. The client came back to the bureau to say that he has now been given an agreed overdraft limit of £2,000. The client has used this overdraft to live on while his benefit payments have gone towards his debts - clearly not a sustainable solution.

26. There are cases in which credit has been given to clients who are suffering from health problems that make their capacity to understand and cope with credit impaired. In these circumstances, lending to these clients could be seen as predatory as the clients may not be in a situation to understand and agree to the terms offered to them.

[2] 'Paying the Price – The real costs of illness and disability for CAB clients' - http://www.cas.org.uk/FileAccess.aspx?id=2980

An East of Scotland CAB reports of a client who came in on behalf of her elderly mother who is registered blind and suffering from dementia. Her mother allegedly entered into a contract with a door step lending agency in 2002 for £200, and again for £300 in 2003. The client believes that her mother never agreed to this and there is no evidence of cash or its disposal. The doorstep lending agency admitted that a loan should not have been made to a person of her age and health.

An East of Scotland CAB reports of an unemployed client with mental health problems who was given a loan of £7,500 from his bank. The client is a qualified social worker who has worked only sporadically for several years. He went to his bank to advise that he was experiencing financial difficulties, and was offered a loan of £7,500, plus insurance, with a total cost of over £11,000 payable over five years. Given the client's unemployment and history of mental illness, the insurance cover would not be suitable for the client. The bureau did not think it was appropriate to offer a substantial loan to an unemployed client with mental health problems and existing debt.

A West of Scotland CAB reports of a client who obtained a credit card from a bank even though she could not read or write. The client got into debt using the card, so had the card cut up. The client came to the bureau in a distressed state after being charged for debts which appear to have occurred after the card had been destroyed. She is being harassed by daily phone calls regarding the debt, but has no surplus income with which to repay. The bureau wrote to the bank explaining that the client cannot read or write due to severe learning difficulties, and that the client therefore did not have the capacity to enter into a credit card agreement. However, the bank is refusing to write off the debt on these grounds.

Older Clients

27. Scottish citizens advice bureau have reported numerous instances of older clients being given credit that is inappropriate for their age and level of income.

28. CAS published the research report, 'Growing Old Together: Older CAB clients and debt'[3] in 2008, which looked at the level and type of debt for bureau clients over the age of 60. The research found that debt clients in this age group have an average debt of £17,767 – an increase of 25% in four years. The research found that older clients are just as likely as any other age group to use credit from credit cards and bank loans.

29. The research found a number of cases in which older clients had been given credit irresponsibly. This includes clients who have been given loans that they are unlikely to repay in their lifetime, as well as clients who were given substantial credit and high credit limits despite only having a small pension to live on.

An East of Scotland CAB reports of a single woman, aged 77, living on a pension of £120 per week. She had two credit cards each with a total credit limit of over £15,000. She had stopped using the cards and been making the minimum payment each month, although this just covers the interest. Recently her credit limit was increased to over £16,000, more than 2.5 times her annual income.

A West of Scotland CAB reports of a 62 year old client employed on the minimum wage who was given a loan of £16,000 by his bank. This loan would be required to be paid well into retirement. The client is now struggling to afford the repayments and is worried about losing his home.

A West of Scotland CAB reports of a retired client who receives calls at regular intervals by her bank offering to "top up" her loan. The client has a number of debts which she believes amount to around £20,000. The client was contacted by the bank suggesting that she "top up" her loan, which she agreed to do, and now has a repayment of £243 per month. The client was unaware that the "top up" was in fact a new loan altogether and as a result she is paying interest on interest. The bureau feels that the bank should be taking the client's multiple debt situation into account each time they offer a new loan.

A West of Scotland CAB reports of an elderly client with non-priority debts totalling over £80,000. The client has 15 store cards, and 9 credit cards. The client has not defaulted on any payments, but rather has been 'borrowing from Peter to pay Paul' and thus adding to his debts. His monthly income consists of his State Pension and work pension. The bureau reports that the client's anxiety about his debts and the possibility of losing his home had made him borrow more to meet at least the minimum payments.

[3] Growing Old Together - http://www.cas.org.uk/FileAccess.aspx?id=5462

30. Older clients are being given loans in situations where they are unlikely to understand the terms and conditions. In some circumstances, this can constitute predatory lending where money is being given to clients who are clearly not in a position to manage credit and debt.

A South of Scotland CAB reports of clients in their late 70's who have been using credit cards to live on and have run up debts to their credit limit. The clients have been naïve in believing that the money was theirs to use and are very distressed and worried about the situation. The bank was negligent in increasing the credit limit time after time knowing that the clients' only income was received from pensions and benefits.

An East of Scotland CAB reports of a client who took out a loan with his bank after receiving loan offer literature with his bank statement. The loan was for £8,856 repayable over five years. The client was 81 years old, and died two years later. His wife has now taken over the repayment of the loan as the bank had insisted that the loan was taken jointly due to the husband's age. She has very little means of affording the repayments and has fallen into arrears.

An East of Scotland CAB reports of an elderly client living alone who has had several loans from a door-step lending organisation. The client is over 65 and should not have been offered a loan according to the organisation's policy. The interest being charged is high and has varied from loan to loan. He has variously been charged 60.49% APR, 440.3% APR, 246.5% APR, 497.4% APR and 596.3% APR. Every time loan re-payments reach completion, a new loan is offered.

Clients with poor credit histories

31. Scottish Citizen Advice Bureau are seeing a number of clients who are being given credit despite already having considerable debt, or in some cases already having a failed trust fund for repaying debt. While this type of practice helps the client in the short-term, in the long term it adds substantially to the client's overall indebtedness.

32. The problem appears to lie in a 'don't ask, don't tell' attitude from creditors who do not check whether clients already have credit and debts from other creditors. In some cases, clients are being given credit despite already having multiple debts with the same creditor.

A West of Scotland CAB reports of a client who is a full time carer who had 16 accounts with various home credit companies. This included seven accounts with thousands of pounds worth of debt with one organisation. The bureau contacted the company to ask why they were prepared to offer seven concurrent loans to a council tenant on income support with substantial debt. They rejected the notion that this constituted irresponsible lending, saying that the client had asked for the money and that was the reason they gave it to her.

An East of Scotland CAB reports of a client with a current trust deed and an extensive history of default who was given a personal loan of £2000 from a finance company. The client has since defaulted on both the trust deed and the personal loan. The bureau felt that the company had offered credit inappropriately to a client who already had a history of defaults, had a trust deed he was already struggling to pay, and yet they still lent him money. This was the second case the bureau had seen in a week in which this company had offered credit to a client who was struggling with a trust deed.

A West of Scotland CAB reports of a client who managed to obtain 13 unsecured loans without the creditors asking if she had any other current loans. The client is a nursing assistant who works full time. She took out £30,000 worth of unsecured loans when she was getting plenty of overtime, but her work has decreased leaving the client unable to service her debts. The client was dismayed at how easy it was to get loans, stating that the banks and other companies had at no point checked if she had any other outstanding credit.

A West of Scotland CAB reports of a client who was given a loan for £3,000 despite already having over £30,000 worth of debt. Already owing some of this money to his bank, he was given the loan without any problems or questions about his other debt. The client now has over £33,000 worth of debt and is unable to repay this amount.

33. Creditors are required to check the credit history of clients before a credit agreement is made, but it is clear that in some cases this either isn't happening or is being ignored. This isn't in the interests of the client or the creditor, as it puts the client in further debt while the creditor is less likely to see a return on their money.

Homeowners

34. Homeowners are being given substantial secured loans on their homes that are disproportionate to their income. In some cases, this lending is such that the secured credit is worth more than the value of the house.

35. This type of lending has serious consequences for clients, as default puts their homes at risk. The size of the lending, and the obvious inappropriateness of the credit to the client's financial situation, implies that companies are authorising these high amounts of credit to homeowners with the understanding that clients are likely to default and lose their home.

> An East of Scotland CAB reports of a client who has secured debt that is worth substantially more than the house. The client bought the house for £60,000 in 2002, and it is now worth around £110,000. Due to financial difficulties, the client re-mortgaged to £77,000 and also managed to get additional secured credit of £79,500. The total secured debt now stands at £156,000, around £46,000 more than the value of the house. The money adviser commented that it must have been evident to the second secured lender that the loan would lead to substantial negative equity and that the repayments were clearly not sustainable from the outset.
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> An East of Scotland CAB reports of a client who was irresponsibly given secured credit based on an inflated valuation of her house. The client has re-mortgaged on a number of occasions, mainly to consolidate debt and the mortgage is now £105,000. In addition, the client has two secured loans totalling £54,000 and a bank loan of £10,000. One of the secured loans was based on a lender valuation of the house of £160,000, when similar properties in the area are being sold for £120,000. The monthly payments of the secured debt amount to £1124 which is only £16 less than her monthly income. The situation will worsen shortly when she comes to the end of the fixed rate mortgage. The bureau believe that the client is very likely to lose her home, and stated that the secured lenders acted recklessly in advancing money when the client's income was already heavily committed.

36. It is likely that the problems caused by excessive lending will increase in the near future, as mortgage and other costs of living continue to increase. More householders will lose their homes as the extent of overborrowing becomes apparent.

Sale of associated products

37. A common problem for clients is their creditor putting pressure on them to take out further products as part of their repayment. Once this offer is in place, it can be difficult for the client to reject the product and negotiate with the creditor. The types of related products that clients can be under pressure to agree to include further loans, consolidation loans, credit cards, and overdrafts.

A West of Scotland CAB reports of a client who made a repayment offer to her creditors, and was instead offered a further loan. The loan would have helped the client to avoid default, but would have cost a further £2700 in interest and charges. The client rejected the offer, and decided to stick to the repayment plan prepared by the bureau.

A West of Scotland CAB reports of a client who was offered a consolidation loan to help her repay her store card debt. The client is managing to make repayments, but the interest and charges applied to her account have meant that her debt has only reduced slightly. The bureau asked the company to freeze interest on the account in order to allow the client to repay the debt, but were advised that this was not their policy. The organisation then contacted the client suggesting that since the client was a home owner, she could apply to another of their companies for a consolidation loan.

An East of Scotland CAB reports of a client who was offered a refinancing loan after making an offer of repayment. The bureau had helped the client to set up a repayment agreement with his bank six months previously with interest frozen on the account. When the arrangement expired, the bureau wrote to the bank with the same offer of repayment as the client's circumstances had not changed. The client then contacted the bureau to say that his bank had contacted him offering a refinancing loan. The bureau explained to the client that the loan would put him more in debt and he would not receive any money.

A North of Scotland CAB reports of a client whose bank will only accept an offer of repayment if the client takes out a new consolidation loan. The client is deeply in debt, and the bureau made offers to her creditors for repayments. The client's bank replied to the bureau saying that they will 'accept' her offer of £175 a month but only if she has a 'new line' opened, ie. takes out a consolidation loan. If the client were to accept this, she would continue to pay interest and charges on the debt.

38. These offers of further products on top of the existing debt seem not to be designed at helping clients to repay their debt, but instead aimed at maximising the amount paid back to the creditor. It is irresponsible to offer clients who already owe often substantial debt further credit, rather than set up a repayment plan to allow the client to repay their original debt.

Account management (including handling of default/arrears)

39. When clients get into their arrears with repayment of credit, creditors have varying policies in response. Some of these policies can help debtors to repay and others can hinder the client, making an affordable loan very difficult to repay.

Interest and charges

40. A creditor's policy on interest and charges on arrears can have a significant impact on the debtor's ability to repay their debt. A common recent policy change for banks is the decision to allow debtors only one short period in which interest and charges can be frozen, before they are restarted and the debt is sold to a debt collection firm. This policy gives the debtor little chance to repay their debts and can have the effect of increasing the value of a debt before it is passed to a debt collector.

A West of Scotland CAB reports of a client who had interest applied to his debt due to a new bank policy. The client has been regularly making repayments of £80 a month towards his debt for around a year. After a review of the repayment schedule, the bank requested an additional £92 a month payment for interest charges. The bank had a new policy of suspending interest for a fixed period of around six months, after which interest and charges are reapplied to the account. The bureau was informed that the account would be passed to a debt collector whether or not the client continued to make payments. The client decided not to make payments until the account reached the debt collector as they will not apply interest. The client then began to receive phone calls late at night from the bank regarding the debt.

A West of Scotland CAB reports of a client whose bank began to add on interest to a debt without warning after a period of freezing interest on the account. The client had been making the agreed £4 repayments to the bank, but was sent a letter stating that the client was now in arrears of £20.73. The bureau called the bank who explained that their policy is to freeze interest for a "once in a lifetime period" of one year. After that interest gets added for 4-5 months, at which point the account will be passed to a collector. The bureau pointed out that the client had adhered to the payment plan and that the interest charges far outweigh what she can afford and she will never make inroads into the debt. This system makes it very difficult for clients to repay their debt, and the policy of adding interest for 4-5 months before passing the debt to a collector only appears to be aimed at maximising the amount owed before the debt is sold on.

Policy on clients in arrears

41. Creditors can also be unhelpful or unsympathetic when a client reports financial difficulties. Common responses include increasing agreed overdraft limits, decreasing credit limits, offering consolidation loans, and in some cases closing the client’s bank account.

A North of Scotland CAB reports of a client who had her account closed by her bank after offering a reduced repayment for her debts. The client is a pensioner whose main source of income is her state pension. The client was having difficulty meeting the repayments on the loan and the bureau made a reduced offer of repayment to the bank and sent the bank a copy of her financial statement. The bank immediately closed her bank account with the result that her state pension which was due on that day seems to be lost. The bank was very unhelpful and would not return calls. The bank eventually offered to open a new account and to try to trace the £380 which has disappeared.

A North of Scotland CAB reports of a client whose bank reduced his credit card limit to below the amount that he owes. The client had reached an agreement with his bank to pay £5 a month for a credit card debt. The credit card had a £3000 credit limit. The client received a letter from his bank stating that his credit limit would drop from that day to £550 – he owed £570.89. In another letter received on the same day he was asked for the full £20.89 limit plus charges.

A West of Scotland CAB reports of a client who received unsympathetic treatment from her bank when repaying her loan. The client has a repayment arrangement in place with her bank that was due to be reviewed in October 2008. The client received a worrying phone call from the bank saying that there is no way that the present arrangement will continue after October and offered a final settlement figure of £9,000 for a debt of around £11,000. They suggested if she did not take advantage of this offer "her house would be involved". Although it was not spelled out, there was a suggestion that the bank was looking for the client to take independent financial advice with a view to equity release on the house in order to take advantage of their final settlement figure.

42. A common response from a bank to a client who is reporting financial difficulty is to increase the amount that a client can effectively borrow, for example by increasing credit limits or authorised overdrafts. This can give a client breathing space in the short-term, but ultimately represents irresponsible lending as the client still cannot afford to repay what they owe and end up with a higher amount of debt. Banks are slow to respond to offers of repayment, but appear to be quick to offer further credit that deepens the amount of debt that a client holds.

A North of Scotland CAB reports of client whose bank continually raised his credit card limit despite his precarious financial situation. The client has never had permanent work, yet has a credit card limit of £11,200. The client was only able to keep paying minimum payments on his credit card debt each month by taking cash withdrawals from his card. As a result of never missing a payment his credit limit was increased on a number of occasions, thereby allowing the client to get into deeper debt.

A North of Scotland CAB reports of a client whose credit card limit has been increased to £7,050 despite the client being unable to maintain payments during the past few years. The client has been on Income Support for 17 years and has a debt of £25,000. She has numerous debts which she has not being paying for quite some years as she is awaiting legal action to allow her to apply for bankruptcy. The bank's reaction to her financial situation has been to extend her credit limit allowing the client opportunity to get further into debt.

An East of Scotland CAB reports of a client who asked for help from her bank in repaying a loan to them. Their response was to raise her overdraft limit substantially. The client had had a series of loans from her bank since the 1980's, which was rescheduled as a £25,000 loan in 2006. When the client returned to the bank for help as she was not able to cope, the bank's response was to raise her overdraft limit from £300 to £2,000.

Scope of Project

43. Bureau evidence shows that creditors can be irresponsible at each stage of the credit cycle, from advertising to handling defaults. It is our view that the OFT's definition of irresponsible lending needs to be as wide ranging as possible to include all aspects of consumer credit lending.

44. In the era of easy credit, creditor policy and practice has encouraged irresponsible lending to a wide range of consumers across various stages of the credit process. Despite the recent slowing of available credit, these policies remain the default setting of the UK financial system.

45. Citizens Advice Bureau clients have experienced a multitude of problems concerning irresponsible lending, including:

- **Advertising and marketing:** Clients have taken extortionate credit based on television adverts making misleading promises

- **Selling techniques:** Salesmen are taking advantage of clients' lack of financial knowledge by offering 'great deals' that turn out to be extortionate

- **Product design:** Credit products are poorly designed for low income consumers, who pay high amounts for credit that can ultimately be unaffordable.

- **Appropriateness of product to borrower:** Low income clients need credit to live, but are receiving unaffordable credit. Credit is being irresponsibly given to vulnerable groups, such as low income clients, older clients, clients with health problems, those struggling to afford their homes, and clients who already have extensive debts.

- **Sale of associated products:** Creditors are selling additional financial products, such as consolidation loans, to clients reporting financial difficulties. These products are often in the interest of the creditor and not the client.

- **Account managements (including handling of default/arrears):** Banks can be unsympathetic to customers reporting financial difficulty, often increasing the amount of money they can borrow rather than finding a solution. Banks can also impose harsh interest and charges on arrears.

46. It is our view that all of the above should be included in the OFT's definition of irresponsible lending. Guidance on irresponsible lending, and on the practices that are considered to be irresponsible, needs to be as full as possible to ensure that consumers know their rights and creditors know their responsibilities.

47. The last 10 years have been characterised by easy and often irresponsible lending to clients who could ill afford to cope with high levels of debt. While we would be concerned if the next few years were to be characterised by a drying up of credit to vulnerable groups in society who often need credit to supplement their low income, we would still like to see creditors acting responsibly by offering credit to those who can repay it at affordable levels. If not, low income clients could be forced to obtain credit from sub-prime creditors where they are likely to be worse off than before.