Citizens Advice Scotland
Scottish Association of Citizens Advice Bureaux

Consumer Credit Review

A Response to the OFT

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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) review of consumer credit. 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 widely blamed for the financial crisis facing the banks and for the record levels of personal debt and consumer credit 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 and poor transparency of pricing to individuals who could ill-afford to hold credit.

6. This consultation response will outline the problems that bureau clients face with the consumer credit sector, showing that creditors can be irresponsible at each stage of the credit cycle. We argue that this evidence shows that the OFT's focus needs to be as wide ranging as possible to include all aspects of unsecure consumer credit lending and its focus shifted from consumer behaviour and decision-making to creditor behaviour and decision making.

Question 2 – We have identified four issues. Are these the key issues?

Consumer Behaviour versus Creditor Behaviour

7. CAS accepts that consumer behaviour and decision making plays a role in consumer credit. However, we believe the focus of a consumer credit review should have another, fifth issue. That issue should be creditor behaviour and decision making. Creditor behaviour impacts both on consumer behaviour and choice. This is highlighted in the initial stages of advertising of a product, selling of the product, and appropriateness of the product to the individual.
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.

11. Scottish bureau advisers often find that clients lack knowledge of financial terms and conditions, and this can prove particularly harmful when dealing with salesmen. Low income consumers may 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.

Selling Techniques

A North of Scotland CAB reports of a client who was falsely told that he would receive 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 and choice 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 misled 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.

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.

Degree of Transparency in Pricing

13. Scottish Citizen Advice Bureaux have dealt with a number of clients who have been misled or accrued debt due to the transparency of pricing. We believe that this is a key area for the OFT to focus on.
14. The transparency of pricing and the level of pricing are key to ensuring that a consumer does not suffer financial hardship, due to over inflated prices for bank charges, account management, third party dealings. Any review by the OFT must monitor this current situation.
15. Overdraft charges, insufficient funds charges and unclear terms have been a hugely significant issue for Scottish bureau clients in the last five years. They are a contributory factor to the increase in the number of bureau clients seeking advice on debt, while bureaux have been active in helping clients to reclaim unfair and disproportionate bank charges. This response will solely look at overdraft charges as other bank charges have been discussed in other consultations to the OFT.
16. A significant finding from the OFT market study is that consumers have a poor understanding of the consequences of going over their overdraft limit. Consumers often underestimate the likelihood of incurring fees and the cost of doing so. Nearly four fifths of consumers in the market study who had been charged in the previous twelve months had never heard of such charges, while only 7% of consumers knowingly went into overdraft.[1]
17. Evidence from Scottish bureaux suggests that clients can have little idea of the likelihood and the cost of incurring overdraft charges. Unfortunately, this is a mistake that can have long-term negative effects for a client.

A South of Scotland CAB reports of a client who incurred bank charges after assuming that his card would be frozen after he ran out of funds. The client did not know about bank charges and thought that he would be told when he had no money. The bureau asked for a refund of charges, but found it very difficult to find somebody who would talk about the client's situation.

18. Our evidence highlights that customers have little understanding of the level and likelihood of incurring charges. The process of charges is unclear and confusing for bureau clients who do not understand the charges until they start to incur them. This raises the question whether penalties and terms and conditions of opening an account are transparent.
19. Scottish bureaux have seen a number of clients who have built up substantial charges for a very small overdraft. These clients often go into their overdraft

[1] Personal Current Accounts in the UK July 2008 - http://www.oft.gov.uk/news/press/2008/84-08

without realising that they have done so, and find that they have incurred high overdraft charges at the end of the month.

20. These overdraft charges are often highly disproportionate to the level of overdraft infringement. This system inherently discriminates against low income customers, where the level of charges is insensitive to the level of infringement. The transparency in pricing for low income groups is disproportionate to the financial penalties incurred for going overdrawn.

An East of Scotland CAB reports of a client with severe mental health problems who quickly built up substantial bank charges for an overdraft of £1.92. The client used her debit card for a purchase of £4.25, not realising that there was only £2.33 in her account. Over the next two months her overdraft of £1.92 grew to more than £180, solely as a result of interest and charges imposed by the bank. The client was very worried as to how she could possibly pay this from an income of £79 per week.

An East of Scotland CAB reports of a client who received excessive bank charges for a small overdraft. The client is a mature student who works part-time. The client went 60 pence into his overdraft and was charged £28 and a subsequent charge of £38. Since then, the client has been unable to clear his overdraft. The client only earns £50 per week, and finds himself in an impossible situation.

A West of Scotland CAB reports of a disabled, lone parent who was given an overdraft charge after exceeding her overdraft limit for one day. The client stated that she regularly checks the status of her account using the telephone services and was at no time made aware of a problem with her account. The client exceeded the overdraft limit on her account for only one day and feels that the £28 charge is excessive and unfair.

21. Overdraft charges can have a significant impact on clients whose only source of income is benefit payments. These clients can budget in pennies, then find that a slight overspend can mean that they owe up to £100 in charges. A standard overdraft charge of £25 can be a daunting prospect for those living on benefit payments.

22. The consequence of this policy is that low income customers can very quickly be in a lot of debt to a bank due to a small overdraft. The customer’s low income would then preclude any chance of getting out of the overdraft, thereby trapping the client in a cycle of debt.

23. The consequence of this cycle of debt is that clients begin to have their benefits –their only source of income- swallowed up by charges. Under the present system, benefits lose their identity when they reach the client’s account, and are used by the banks for paying bank charges. This can leave clients with very little to live on.

An East of Scotland CAB reports of a client who opened a student account upon starting her studies, and built up substantial charges without ever using the account. At some point, the client’s account changed to a ‘royalties account’ which meant a charge of £6 per month for use of the account. Because there was a zero balance the £6 charge put the account into the red and a £28 per month bank charge plus interest began to be applied. By the time the client realised what had happened, she had a debt of over £300 and rising. The client maintains that she was not told that the unused account was going to be upgraded to the new fee-charging account nearly two years after she had initially opened the account.

24. Clients need to take responsibility for knowing how their current account works and the charges for its misuse. However, banks have a responsibility for ensuring that the terms and conditions of use for current accounts are clear and understandable. This is not always the case. The OFT market study raised concerns over a 'lack of transparency' over 'less visible' terms and conditions in current accounts. This is borne out in Scottish bureaux evidence.