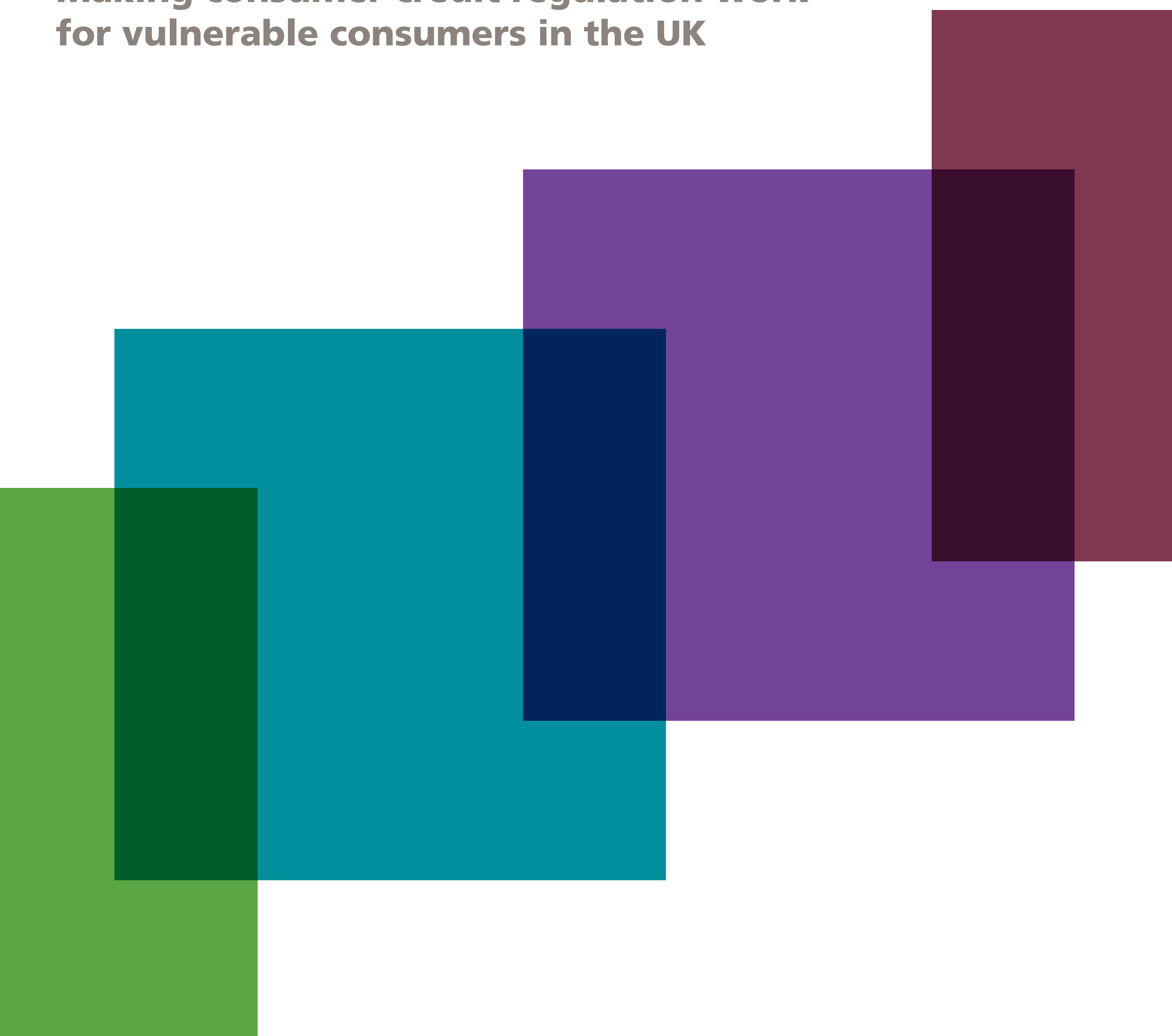
citizens advice bureau

A credit to the nation?

Making consumer credit regulation work for vulnerable consumers in the UK



Summary

Consumer credit is vital to the economy but it is also one of the biggest causes of issues raised with the Citizens Advice service. Over the last four quarters, Citizens Advice Bureaux in England and Wales have dealt with more than two million problems about debt, 41 per cent of which were consumer credit related. Debt problems overall represented 30 per cent of all problems.

There is great scope for consumer detriment where credit and debt is concerned, from a payday lender emptying an individual's bank account to a family losing their home because poor advice from a debt management company meant they paid non-priority debts instead of the mortgage. Issues with consumer credit can also have a significant impact on consumers' health – with increased stress causing both physical and mental health issues – and family life.

The regulatory structure for financial services is changing and responsibility for consumer credit regulation is moving to the new Financial Conduct Authority (FCA). This is an ideal opportunity to give consumers more protection from unscrupulous companies and highly questionable practices which cause significant detriment.

Developing a new regulatory regime for consumer credit – one that is firmly focused on consumers – raises a number of important questions for consideration:

- What do consumers need from an effective regulatory regime?
- Which elements of the current regime should be retained?
- How will the regulator need to adapt its approach to be able to deal with the consumer credit market?
- What outcomes do we want to see?

Evidence from the Citizens Advice service shows the nature and scale of the issues consumers experience now and these issues should be used to help shape a stronger more effective regime for the future.

Introduction

The entire regulatory landscape for financial services is changing to strengthen regulation and address the issues with the current structure. A single regulator is being split into three. One of these regulators – the Financial Conduct Authority (FCA) – will have an objective to protect consumers. These changes are being introduced in the Financial Services Bill, currently being debated in Parliament.

As part of this regulatory overhaul, the Government has announced plans to transfer responsibility for the regulation of consumer credit from the Office of Fair Trading (OFT) to the new FCA. Amendments to the Financial Services Bill to make this happen have been agreed by Parliament. Once the Bill becomes law, all that remains is the mammoth task of designing and building the new regulatory regime – and, most importantly, making sure it works for consumers.

The importance of consumer credit to the economy

As the Government said in its consultation[1] on the future regulation of consumer credit:

> 'Consumer credit is vital to the UK economy. It funds the purchase of goods and services and provides people with greater flexibility with their spending. A healthy consumer credit market which serves businesses and consumers well is central to economic recovery and growth; and a key element of a healthy consumer credit market is effective regulation.'

We don't need to look far to see just how important consumer credit is. At the end of August 2012, the total amount of unsecured debt in the UK was £156.6 billion[2]. At the same time, average household debt (excluding mortgages) was £5,949[3]. In 2011 there were 54.5 million credit cards[4], 62 per cent of the adult population have a credit card and credit and charge cards were used to make 2.1 billion purchases to the value of £140 billion.

Getting regulation wrong would have a big impact on both consumers and the economy more generally. But getting it right is vital to improve the experience of the consumers, particularly those on lower incomes and more vulnerable consumers, who seek help from the Citizens Advice service. Debt issues are common with consumers who visit bureaux. In the second quarter of 2012/13, Citizens Advice Bureaux in England and Wales dealt with 495,000 debt problems, including more than 65,000 issues with unsecured loan debts, such as payday loans, and more than 60,000 issues with credit and store card debts. The total of debt issues represented 30 per cent of total issues raised over the year, the second most common issue raised with bureaux. Citizens Advice has produced numerous reports highlighting consumer detriment caused by the practices of consumer credit firms – such as *Cashing in* which highlighted the menace of upfront charging by credit brokers, *Out of order* which highlighted the use of charging orders and orders for sale in debt collection and *Set up to fail* which looked at problems with mortgage and secured loan arrears. Questionable practices which are designed to take advantage of vulnerable and less informed consumers continue to evolve and spread.

1. A new approach to financial regulation: consultation on reforming the consumer credit regime, HM Treasury and BIS, December 2010
2. Bank of England Statistical Release, September 2012
3. Credit Action, Debt Statistics, October 2012
4. UK Cards Association

What would make the new regulatory regime work for vulnerable consumers?

The Consumer Credit Act 2006 introduced 'once in a generation' changes to the regulation of consumer credit and gave the OFT a range of new powers, including the power to impose requirements on consumer credit licence holders and to impose civil penalties of up to £50,000 on licence holders for a breach of requirements, but these have failed to tackle the problems faced by consumers, particularly vulnerable consumers. Evidence from the Citizens Advice service shows that questionable practices from consumer credit firms continue to have a detrimental impact on consumers, affecting not only their financial situation, but also their mental and physical health and family life. We believe that there are three fundamental reasons why the current consumer credit has performed relatively poorly and ensuring credit markets work well for consumers:

- The legislation does not provide the OFT with sufficient controls on firms entering the consumer credit market.
- The OFT does not have positive prior control on either conduct of lenders or consumer credit products entering the market.
- The CCA does not give the OFT sufficient policy autonomy.

Nor does the OFT have the resources necessary to tackle these widespread and systematic bad practices by consumer credit firms that bureaux see. The maximum charge for a consumer credit licence is £1,215, payable on application or renewal, providing the OFT with £11.5 million of income in 2011/12[5]. The overall budget for regulation by the OFT is set by the Government. On the other hand the FCA will be able to levy regulated firms to meet the costs of regulation.

A new regulatory regime and a new regulator with increased resources is a real and exciting opportunity to shift the focus to protecting consumers. The Government talks about developing a proportionate regime but has not defined what proportionate is. Additional costs to business must not be given more weight than consumer protection. It is also important that the new regime includes some of the key consumer protections which are part of the current regime.

The recent FSA publication, *Journey to the FCA*, is an encouraging start for the new regulatory regime as a whole and the interests of consumers have a higher billing than has ever been the case before, for example:

> 'We would expect the sorts of standards that consumers associated with basic vehicle safety…to be the norm for widely sold financial products'
>
> '…take into consideration the potential scale of harm to individual consumers and whether issues may lead to harm for particular groups of vulnerable consumers.'
>
> '…we will not let a firm compromise fair treatment of customers to achieve financial success.'
>
> '…we will go further than the FSA has previously done in challenging providers on the value-for-money of their products…'

We agree with the statement that 'The creation of the FCA is our opportunity to reset conduct standards for the financial services industry'. This is a worthy intention which must be carried through and extended to every part of the new regime.

Developing a regime to achieve this for consumer credit raises a number of questions for consideration and debate. It is encouraging that the FSA says it will 'work closely with consumers, the industry and Government to develop proposals for effective regulation' of consumer credit. But what does that mean in practice? We think that there are four key questions that the FCA needs to address for that approach to work.

5. OFT Annual Report 2012

1. What do consumers need from an effective regulatory regime?

Transparency of terms, conditions, outcomes and charges, transparency about who the regulator is and where to go if things go wrong

Transparency is important to help consumers understand what they can expect from products, what they can do if they get into financial difficulties and who they can go to for help if they need it.

Improved transparency would help tackle issues around bill of sale loans, for example. A bill of sale loan is a way of raising money by offering an item of personal property as security for a loan. The bill of sale agreement effectively passes over ownership of goods to the creditor. As long as payments are maintained, the borrower can keep the goods. If the borrower defaults, the creditor can repossess the goods without a court order.

This type of lending is not new – the legislation dates back to Victorian times – but has seen an increase in recent years. These loans are high cost, sub-prime and often targeted at financially vulnerable consumers, including those already in financial difficulty. Default charges and high interest rates can cause debts to spiral, often leaving borrowers with an unmanageable debt. In some cases the borrowers do not understand the potential implications of a bill of sale loan – that there is little the borrower can do to stop repossession if they default on payments. Detailed rules on the information to be provided to customers should help consumers understand more about what they are getting into.

> A CAB in the East of England reported seeing a man who was unemployed, homeless and claiming jobseeker's allowance. When working he took out a loan secured by a bill of sale on his car but was unable to keep up the payments following the loss of his job. Initially the company had agreed to a revised payment schedule but they then asked the client to increase the amount to a sum he could not afford. An officer from the company visited the house where the client was staying and threatened to take his car. The client had not understood that the loan company owned the car until the loan was repaid and if he defaulted he would forfeit the car.

Lack of transparency can also be a problem with payday loans. Many payday lenders collect repayments via continuous payment authorities (CPA) – a way of using a consumer's debit card details to take repeated payments from their bank account. CPAs do work for some consumers. But poor understanding of what CPAs do – allowing the lender to take money from the borrower's bank account – together with misuse of this form of payment causes consumer detriment.

> A CAB in North East England reported the case of a young single woman who lived with her parents. The client had run up debts to various payday loan companies following a relationship breakup when she had borrowed money for her ex-partner in her name. Various payday loan companies had continuous payment authorities in place but the fact that these gave access to the client's bank account was not explained to her. When the client couldn't afford to pay back the loans on the due date they took varying amounts over several days. One of the companies accessed her bank account on seven different occasions over Christmas 2011 to take amounts varying from £5.10 to £857, totalling £1453.75 over four weeks. The client had virtually no income as a result of this and incurred charges. The client found herself 'churning' her payday loans and taking offers of 'rollovers' which got her even deeper into debt.

Consistency of regulation

A detailed rule book – rather than a principles based approach – setting out clear requirements together with effective supervision of firms should help ensure regulation is consistent across different types of firm. The rule book must be very detailed to remove any wriggle room for unscrupulous firms and to cover the wide diversity of the consumer credit market. Regulatory action needs to be less dependent on complaints and triggered before consumers experience detriment.

Currently, the OFT issues comprehensive guidance, under section 25A of the Consumer Credit Act, covering areas such as irresponsible lending and debt collection practices. The guidance is intended to provide clarity for consumer credit licence holders about what is expected of them in order to show they are fit to hold a consumer credit licence. All holders of consumer credit licences are supposed to follow this guidance. Despite this, the Citizens Advice service sees continued non-compliance with the OFT guidance. For example payday lenders are failing to lend responsibly. The OFT review of payday lenders' compliance with the irresponsible lending guidance[6] shows the widespread concern that lenders are flouting the guidance. People with very low incomes, or even no income in some cases, are able to obtain payday loans at very high interest rates, and often more than one loan at a time. Customers who are unable to repay loans when they are due can then be offered the facility to extend or 'roll over' their loan. This practice results in the borrower's debt ballooning with high levels of interest and other charges. This causes the client's debt to become unmanageable as they struggle to maintain payments to service the loan, causing a cycle of debt which is difficult to break.

A CAB in the East of England saw a woman who had an ongoing multiple debt problem and had resorted to payday loans several months earlier as a short term solution. She was borrowing an average of £400 a month in payday loans. At the end of each month the lender sent her a text message asking how much money she would like transferred into her account that day. As the client was struggling to maintain her current payments to her debt management company she was easily tempted by the text messages to borrow more money each month.

A CAB in the South of England reported the case of a man who was a stay at home father to three daughters aged 8 years, 6 years and 18 months, while his wife worked from 7am-7pm daily. Shortly before the client unexpectedly lost his job his wife had taken out a payday loan of £345. They were now unable to repay the whole amount. The client had offered to make smaller payments but had been refused and the interest kept rising. The man told the bureau he was getting up to nine telephone calls a day from the payday loan company and, when he complained of harassment he was laughed at.

Protection against targeting of vulnerable consumers

Higher barriers to entry – such as a requirement for key individuals in a firm to be approved and greater scrutiny of business and product plans – would reduce the profusion of firms that are not in the market for the long haul and who pay little attention to the needs of their customers or good standards of business conduct.

Currently, the main grounds on which the OFT can refuse a credit licence is that the individual or firm is not fit to hold a licence. The Consumer Credit Act 2006 did give the OFT some powers to look at new entrants and there is a process in place for increased scrutiny of high risk entrants – such as debt collection – but low barriers to entry result in consumer detriment rather than a competitive market.

Recent examples of consumer detriment have included online credit brokers who have deducted administration fees, for finding a loan, from individuals who visit their website but ultimately don't sign up for their service. Bureaux also report cases of firms

6. OFT Press Release, February 2012

misusing people's payment details to take unauthorised payments – causing significant consumer detriment – from the client's account.

> A CAB in the South West of England saw a woman who had searched the internet for information about loans. She came across a credit broker and started to complete an online application. However, she discovered that the broker would take a fee of £69 so she abandoned the application. Soon afterwards she received a phone call from the broker saying that she must pay the fee to get a loan. She told them that she did not want the loan and did not want to proceed. The agent on the phone confirmed this was not a problem. She was therefore surprised when the £69 fee was taken from her bank account. She had tried to call them again but they never answered the phone.

Product intervention powers

Under the provisions of the Financial Services Bill, the FCA will have new powers to ban products which are unacceptably risky for consumers, subject to consultation. The FCA will also be able to introduce temporary rules to ban products where a delay due to consultation would damage consumer interests. Neither the OFT nor the FSA have similar powers currently and these powers are a welcome and essential move to help reduce consumer detriment. In our experience, issues result from the fact that firms create very attractive offers – such as the free travel insurance which comes with some packaged bank accounts – and develop well-scripted sales processes which focus entirely on making the sale rather than meeting the needs of customers.

> A CAB in the South West of England reported seeing a man who had taken out three logbook loans but was struggling to meet the repayments. The man lived with his partner and adult son in local authority rented accommodation and relied on a state pension and other benefit income. When he went to the bureau the man had three loans of £500 each, totalling £1,500. The loan company had continued to offer him loans even though he was struggling to make the repayments. He thought he had paid back £3,270 but still owed £4,200. The man was expected to make repayments of £120 a week which he could not manage. He was anxious about making the repayments and was becoming depressed.

Tougher controls on financial promotions

More and stricter controls on financial promotions should help ensure that consumers are given all the information before they sign up for something and that companies cannot make unrealistic claims about the services they offer, such as debt management companies claiming to be able to write off debts. The differences between the current OFT and FSA regimes are telling. While credit advertising is regulated currently, and there are specific requirements about the information which must be given, the requirements do not extend to all consumer credit services – such as debt management – and the information provided can be confusing for consumers. On the other hand, the FSA requires all financial promotions to be fair, clear and not misleading. Where promotions do not meet these requirements, the FSA can require the promotion to be changed or removed and can direct the firm to contact consumers who might have been misled and provide redress if they have lost out as a result. These powers will be strengthened under the new regime.

> A CAB in the North of England reported seeing a woman who was working but on a low income. She was struggling to manage her priority payments and was behind with her rent, gas, electric and water. She approached a debt management company about four non-priority debts totalling more than £5,000. The company set up a debt reduction plan for £100 a month – unlike a debt management plan where the objective is to repay debts over a period of time, the purpose of a debt reduction plan is to reduce the overall amount owed, for example by reclaiming PPI or bank charges or having credit agreements declared as

unenforceable. However the client was not given full debt advice dealing with all her creditors and all possible options available. Paying £100 a month to a debt management company meant she could not afford her priority bills and had no money for food.

CAB evidence highlights many cases were people have been induced into inappropriate or unaffordable credit agreements by means other than advertising in the strict sense. Problems include:

- evidence of people being offered inappropriate credit by lenders' staff directly, often on visiting a branch and often in response to a request for help with financial difficulties

A CAB in the North West saw a man who was in arrears with his mortgage. He told the CAB that when he had approached his mortgage lender for help some time earlier, they had recommended that he should increase his overdraft and take out a credit card with a credit limit of £7,000 to top up his wages. By the time he sought advice, the client owed £2,000 on his overdraft and £7,000 on his credit card as well as his mortgage arrears. Having asked for help as soon as he was aware that he was potentially in difficulty with his mortgage, the client's situation worsened because the bank sold him additional inappropriate products.

- growing evidence of poor outcomes from online sales of credit agreements.

A CAB in the Midlands saw a couple who had three children and were both working full time. They had built up £120,000 of consumer credit debt spread over 28 credit cards, bank loans and store cards. They had not understood their financial position and had taken on more and more credit without considering how repayments would be made. They said that firms offering 'easy' credit made it sound so simple so they took on the debt without realising the long term implications. They developed a false sense of confidence because the credit card providers and the bank loan providers allowed them to take on more and more credit. The husband had a period off work with ill health and this revealed the difficult situation they were in. They were under enormous strain. Their only option might be bankruptcy and the likelihood was that they would lose their home.

A CAB in London saw a woman who had taken out a £250 loan online for an emergency flight. She was unaware of the terms and conditions of the loan as these were not made available until her full details were passed to the lender in the application process. She did not make the repayment on time and the debt racked up to over £400 in a matter of weeks. She tried to negotiate reduced payments but the lender refused to cooperate and was harassing her, by suggesting they would tell her employers.

Effective redress

A regulator with the power to order consumer redress should see redress being paid to consumers who have suffered detriment without the need to pursue an individual complaint through a lengthy process, which can put some consumers off. The power to order a redress scheme to compensate all customers affected would also act as a deterrent against poor practice.

Currently the OFT can revoke consumer credit licences or place requirements on a licence. This protects future customers but does nothing to help consumers who have already suffered detriment as a result. A good example of this is the case of the sub-prime first and second charge mortgage lender Swift. Investigations by the regulators found that Swift was giving secured loans to customers with poor credit histories or limited access to credit without checking whether they could afford the loan or verifying their income and was not explaining charges fully to customer. The OFT imposed requirements on Swift's consumer credit licence[7] but the FSA were able to fine Swift £630,000 for the unfair treatment of some customers with mortgage arrears and also directed the firm to pay redress to customers who were affected[8].

7. OFT Press Release (23 June 2011)
8. FSA Press Release (8 September 2011)

2. Which elements of the current regime should be retained?

The current regulatory regime for consumer credit includes some important elements of consumer protection which are not replicated in the legislation which set up the Financial Services Authority[9]. Citizens Advice believes it is essential to retain some key protections.

Equal liability (usually referred to as section 75)

Where there is a breach of contract, such as unsatisfactory goods, and a regulated consumer credit agreement is involved, the credit provider may be liable as well as the trader. The provisions – under sections 75 and 75A of the Consumer Credit Act – mean that where there is a problem with the goods or services bought on credit, the consumer may be able to seek redress from either the trader or the credit provider or both, giving the consumer a better chance of getting the issue resolved.

The standard protection (section 75) applies where the cash price is between £100 and £30,000. More limited protection is available under section 75A (which implements the Consumer Credit Directive or CCD). This applies where the cash price is more than £30,000 and the amount of the credit agreement is not less than £160 or not more than £60,260 but the consumer must pursue the supplier first before pursuing the creditor (in contrast to section 75 where the consumer can go to either the trader or the credit provider) and the credit must be linked to the goods or service (so does not apply to credit cards). When the Government implemented the CCD, it retained the important consumer protection offered by section 75. There is no case to reduce that protection now.

A CAB in Wales saw a man who had signed up with a training company to do a course in computer engineering. The course offered online training sessions, books, CDs, examinations and help to get employment in the field. The total fee was £4,900 which the client had been paying by a linked loan. The client wanted to do the course as he had been made redundant from a higher paying job and now worked in a food processing plant. The client was unhappy with the quality of the course and had taken no exams despite regularly contacting the trainers about it and always getting prevarications and evasions. He had found hundreds of complaints about the company on social media websites.

When the training company had ceased trading, the finance company contacted him to tell him that they had arranged for another training company to take over the course, but the client had received no further details as to whether the new company would actually provide the training he needed. The CAB advised the client not to stop paying; give the new course a chance – and if it was unsatisfactory, write to the finance company reminding them that under Section 75 of the Consumer Credit Act 1974, they had joint liability with the training providers to offer a suitable course. Alternatively, the client could choose another course and claim the fees from the finance company. He could also claim damages for the level he should be at.

9. The Financial Services and Markets Act 2000 only gives consumers the right of private action if a firm breaches a rule

Time Orders

Sections 129-136 of the Consumer Credit Act 1974 allow consumers to apply for a time order to reschedule payments under a consumer credit agreement. Time orders are most useful where:

- the consumer is likely to lose an asset as a result of short-term financial difficulties; and
- the original agreement was harsh on the consumer and he or she was disadvantaged in negotiations or ignorant of its implications.

Currently not all consumers have the protection of time order provisions, for example the protection is not available for first charge mortgages. The new regulatory regime is an opportunity to ensure that this protection is available to all borrowers.

A debt purchase company issued bankruptcy proceedings for a debt even though they already had security by means of a court judgment and a charging order. They would not accept a reasonable offer of payment from the debtor and communicated with him in an intimidatory manner, including slamming the phone down on him. The debt purchase firm also would not cooperate with requests for information, including providing a breakdown of the costs of the debt. The client wished to avoid bankruptcy, as he could have lost his home, his reputation in the local community and his position as a member of the management committee at a local working men's club. The adviser was able to obtain a time order in court prior to the bankruptcy hearing. The creditor's bankruptcy petition was dismissed by the district judge, who commented that the behaviour of the creditor was very heavy handed and oppressive and he advised their representative to take this advice back to them.

Unenforceability of credit agreements

Where a credit agreement is regulated under the Consumer Credit Act, the Act specifies rules which the credit provider must normally follow, such as providing information to help the consumer understand the agreement. If the provider fails to follow these rules, the agreement may not be enforceable without a court order under section 127. There are more severe sanctions for lenders where the agreement was taken out before April 2007. The irredeemable unenforceability provisions which apply to those agreements are a sanction against lenders who do not provide the most basic and essential information to borrowers.

A CAB in the East of England reported the case of a client who had catalogue debts of £3,400 with two different catalogue companies. She believed both accounts were taken out in April 2006. As the accounts were opened prior to April 2007, in order to enforce the debt, a consumer credit agreement must have been signed by the client and be produced by the creditors when requested. One company conceded that the debt was unenforceable. The second company responded that the account had been opened in 2008. This would mean the debt was enforceable. However there appeared to have been a transfer of a balance from an existing, older account, suggesting that the company set up the new account and transferred the balance from an earlier account in order to avoid the enforceability issue. When the bureau queried the balance transfer and asked for a signed credit agreement, the company responded that they would not pursue the debt any longer.

Citizens Advice believes the current unenforceability provisions provide important consumer protections. They help ensure that lenders draw up agreements properly and that consumers are not misled or placed at a disadvantage and act as a deterrent to unscrupulous lenders. The unenforceability provisions provide a remedy for consumers that damages alone would not. The court must retain the power to ensure that consumers get the right relief where the creditor has not followed the rules on form and content of pre-contractual information and credit agreements.

Illegal money lending

Section 39 of the Consumer Credit Act provides that trading without the right sort of licence is illegal, and under section 40 any loans made by a trader lending without the right sort of licence cannot be enforced except with leave of the OFT. In comparison, whilst section 19 of the Financial Services and Markets Act states that trading without authorisation is illegal and any agreement made by the unauthorised person/firm is unenforceable, section 20 states that trading without the correct permission is not an offence, and does not make agreements unenforceable.

We believe that sections 39 and 40 of the Consumer Credit Act provide important protection for consumers against illegal lending and debt collection activities. Regional teams of experienced trading standards officers and enforcement officers have been established to enforce these provisions, by investigating and gathering intelligence about the activities of unlicensed, illegal money lenders and prosecuting them. They also recover assets from convicted illegal money lenders and provide support to the victims of loan sharks.

Citizens Advice strongly supports the work of these illegal money lending teams and we believe they should continue. It will be crucial for the FCA to work effectively with these teams to tackle the issue of illegal money lenders.

A CAB in London reported the case of a client who had been unable to work as a result of injury and had a significantly reduced income living entirely on benefits. The client's wife had taken out a £500 loan from a local loan shark to buy Christmas presents for their grandchildren. The client did not have an agreement from the loan shark, he did not know how long it would take them to pay the debt or how much interest was being charged. All he knew was that they had to pay £5.00 a week. The client said he knew the debt was illegal but the loan shark was well known in the area and the client would not report him because he could 'have his house burnt down'.

3. How will the regulator need to adapt its approach to be able to deal with the consumer credit market?

The consumer credit market is very different to other markets regulated currently by the Financial Services Authority (FSA), the predecessor to the FCA. As such the regulator will need to adapt its approach.

Citizens Advice believes a detailed rule book is essential to help eliminate many of the issues raised by bureaux clients. The OFT has already taken steps to tackle some of the causes of consumer detriment, for example OFT guidance on debt management and debt collection have recently been updated to take account of changes in the market.

But the impact of these changes has been limited due to:

- continued non-compliance with OFT guidance
- the time needed to make changes in order to tackle emerging new practices
- the high level nature of some of the provisions.

With the transfer of regulation to the FCA, these issues and other causes of detriment could be eliminated because the regulator would be able to set out explicitly what firms must and must not do, giving earlier positive initiatives the strength of rules, backed by a regulator with sufficient enforcement powers to ensure even the largest firms took note.

There are numerous examples of current consumer detriment where firms do not comply with existing guidance and where bureaux see new practices emerging which are not in the interests of consumers.

Recent emerging practices seen by the Citizens Advice service include numerous cases of credit brokers taking upfront fees and other charges from consumers, with the promise of finding them a loan. In many cases, that promise is not fulfilled and the consumer is worse off after paying the fees. Some consumers have their contact details passed around a number of firms or brands, resulting in contact from different companies (often unsolicited and confusing for the customer). This is contrary to the OFT guidance for credit brokers which cites both failure to be clear about fees to borrowers and any suggestion that credit will be available regardless of status as unfair practices[10].

> A CAB in the East of England saw a lone parent with historic debt problems and a poor credit rating. The client had wanted to take out a loan for £500 to pay an urgent demand for water arrears. He contacted one company (who he assumed was a lender but was actually a broker) who charged him a 'membership fee' of £49.50 but did not arrange a loan. When he contacted the company again about trying for another loan, they referred him to a different company and gave him a phone number which he called. He was then emailed an application form. He completed the form and was given a 'green light' which he assumed meant a loan had been agreed so he provided his bank details. A little later he found that £69.50 had been taken from his bank account but, again, no loan has been forthcoming. The client was sure that there was no mention of a £69.50 charge at any time during the initial phone call, in the email, or on the application form. He had thought that the company was a lender, but some quick research on the internet established that it is another loan broker. The client struggled to manage on a low income and to pay £119 for nothing was no small matter for him. He felt misled and exploited by the two loan brokers.

The gaps in the current regulatory regime also leave room for scams to develop and credit broking is a vehicle which can be used for pure scams. Cold calling and upfront charges present opportunities for fraudsters. Cold calling in itself can make it difficult for consumers to work out what is a scam and what is legitimate.

> A CAB in the South West of England saw a client who was called by a company, who he believed had been passed his request for a loan by a credit broker who he had a broker agreement for a loan with. Over several phone calls the client paid £543 in total for differing upfront fees to the company who contacted him, before he refused to pay any more before taking advice. The scam was very well executed verbally, but poor emails from them alerted the bureau that it was a scam. The client had taken out payday loans to pay for the upfront fees demanded by these scammers and had paid by cash.

10. OFT Guidance for brokers, intermediaries and the consumer credit and hire businesses (November 2011)

4. What outcomes do we want to see?

The new regulatory regime needs to be focused firmly on outcomes for consumers, who are less concerned about process and more concerned about what happens for them.

A proactive regulator dealing with issues before widespread consumer detriment occurs

A proactive regulator is needed to deal with the increasing number of issues with payday lending being reported by bureaux, such as customers who are unable to repay loans when they are due being offered the facility to extend or 'roll over' their loan. This practice results in the borrower's debt ballooning with high levels of interest and other charges, and can cause the client's debt to become unmanageable as they struggle to maintain payments to service the loan, causing a cycle of debt which is difficult to break.

A proactive regulator could also deal quickly with new practices and firms which emerge, such as debt management firms charging for help with bankruptcy but not doing very much for the client.

> A caller to the Citizens Advice consumer helpline said a firm had contacted him a few months before about bankruptcy. The client had paid £1,200 but was unable to contact the firm. He had not given been given any paperwork and the bankruptcy papers had not been lodged with the court.

Controls on firms entering the market which prevent unscrupulous firms from ripping off consumers

As the evidence in this report shows, there are many areas of malpractice in the consumer credit field which impact upon consumers. Some of the biggest causes of consumer detriment come from debt management and credit broking. Another persistent and damaging practice is that of unfair and heavy handed debt collection. The regularity with which this occurs and the human suffering it engenders are difficult to overstate.

A significant problem with debt collection is creditors and collectors ignoring good practice standards and going hard after people in financial difficulties. Harassment by frequent call and/or text messages is a common issue reported by bureaux. Citizens Advice evidence includes cases where debt collectors pursued individuals relentlessly at their workplace, putting their employment in jeopardy, spoke to family and neighbours about the debt or tried to collect a debt in wildly inappropriate circumstances.

> A CAB in the East of England saw a woman who was unable to work due to illness which restricted her physical capacity. Some days she was housebound and she had been struggling to maintain her payments to her creditors. A debt collection company was collecting the debt for one of her old catalogue creditors. The company called her continuously, up to ten times a day, and demanded higher payments than she could afford. The bureau gave her a creditor harassment factsheet to help her. When the debt collection company called again she quoted the OFT guidance and said that she felt she was being harassed by the nature and number of calls. The company said 'We can call you as many times as we like until this is resolved.' They continued to threaten to 'send the bailiffs round'. The client was terrified that bailiffs would visit her. She was so distressed by the large number of threatening and bullying calls made by debt collection company that her doctor had to increase her medication and put her on anti-depressants.

Effective deterrents to help ensure firms do the right thing

While the OFT can revoke a consumer credit licence in some circumstances, it is unlikely they would ever attempt to remove the licence of a major bank or credit card provider. And even if the OFT did impose requirements on a firm, the maximum penalty of £50,000 for non-compliance is an insufficient deterrent for a large multi-national company and relies too heavily on a very large number of customers, or their advisers, being willing to provide evidence to the OFT about the breach.

The new regime must enable firms to be monitored more closely, face more realistic fines and other financial consequences – such as paying redress to customers – when they are found to be breaking a rule or principle. A fine of £1.5m, the amount the FSA fined Santander for failing to clarify FSCS cover on structured products, would have much more of a deterrent effect[11].

Effective redress when things do go wrong – ordered by the regulator when an issue is identified

Despite recent enforcement action by the OFT, Citizens Advice continues to see problems with fee-charging debt management companies. Evidence from bureaux shows that people using these companies continue to face a number of problems leading to severe detriment. Recent cases reported by bureaux include:

- pressure selling, such as cold calling, unsolicited texts and refusing to observe cancellation rights
- misleading information and poor advice
- poor service, such as failing to pass on payments to creditors and not dealing with the most important priority debts
- lack of transparency around fees, large upfront fees and management fees that are disproportionate to the reduction in debts
- failing to keep client money safe.

In June 2012 a CAB in the Midlands saw a lone parent with four children. The client was unemployed at the time and went to the bureau to seek advice about multiple non-priority debts. The client had been cold called by a debt management company, after which the she agreed to make a payment of £210, which the client was informed was an administration fee, as well as further monthly payments of £163 towards the debt management plan. The client agreed to this plan despite being up to date with her payments. The combined effect of the upfront fee and the unsustainable monthly payments meant the client was unable to maintain payments towards her debt and was forced to seek advice from the bureau about an application for a debt relief order.

A CAB in the Midlands reported seeing a man who was married and living with his wife in a property which they were in the process of buying. The man was working as a self-employed taxi driver, and his wife worked part-time in a supermarket. The couple had signed up with a debt management company in the hope of sorting out their debts of approximately £42,000. The company charged an initial management fee of £450 and the couple then started making payments of £425 per month. Of this, £106.25 (25 per cent) per month was deducted by the debt management company in service charges. This left £318.75 per month to be distributed amongst creditors. The combination of these fees resulted in the couple losing £900 in only five months, which could have been better spent by paying off the debts which this company were supposed to be managing. As a result, the couple were worse off financially.

11. FSA Press Release (20 February 2012)

A reduced need for consumer organisations to make super complaints

Under the provisions of the Financial Services Bill, Citizens Advice will be able to make super complaints to the FCA, as we can do now to the OFT. A super complaint is a mechanism which allows Citizens Advice and some other consumer bodies to complain about elements of the market which cause detriment to a large number of consumers. Two out of the three super complaints Citizens Advice have made have been about financial services. One of the most valuable measures of how effective the new regulatory regime is will be the number of super complaints made by Citizens Advice and other organisations. The ideal result for consumers must be a vastly reduced need for super complaints.

Where next

Many of these issues have been debated in some depth during the passage of the Bill through Parliament and it is vital that the Government does not water down commitments made to date, such as to keep key elements of consumer protection from the Consumer Credit Act[12].

As the chairman of the Treasury Select Committee said:

> 'The creation of the FCA is an opportunity to create something much better. If we are not careful the FCA will become the poor relation among the new institutions. But it is the one that will matter most to millions of consumers'[13]

The Government has been clear that the transfer of consumer credit regulation will take place only if a proportionate regime can be developed, but what is proportionate has not yet been defined. Costs to business cannot and should not be given more weight than the interests of consumers.

Citizens Advice Bureaux have seen widespread consumer detriment in the consumer credit market. Now is the time to tackle the causes of that detriment and build an effective regulatory regime which really works for consumers.

12. Hansard, 23 Apr 2012, Column 694
13. Treasury Select Committee Press Release (13 January 2012)

Our aims

- To provide the advice people need for the problems they face.
- To improve the policies and practices that affect people's lives.

Our principles

The Citizens Advice service provides free, independent, confidential and impartial advice to everyone on their rights and responsibilities. It values diversity, promotes equality and challenges discrimination.

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Citizens Advice is an operating name of The National Association of Citizens Advice Bureaux.
Registered charity number 279057.

November 2012