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

Consultation Paper
CP18/12***

May 2018

How to respond

We are asking for comments on this Consultation Paper (CP) by 31 August 2018.

You can send them to us using the form on our website at: www.fca.org.uk/cp18-12-response-form.

Or in writing to:
James Eldridge
Financial Conduct Authority
25 The North Colonnade
London E14 5HS

New address from 1 July 2018
Financial Conduct Authority
12 Endeavour Square
London E20 1JN

Telephone:
020 7066 9280

Email:
cp18-12@fca.org.uk

How to navigate this document onscreen

returns you to the contents list

takes you to helpful abbreviations

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This table sets out which chapters are particularly relevant for each sector. This is where you will find the most relevant chapter(s) for your firm.

1 Summary

Why we are consulting

1.1 High-cost credit is used by over three million consumers in the UK, some of who are among the most vulnerable in society – with low credit scores and with typical income levels, including benefits, between £15,500 and £18,000. Ensuring appropriate protection for these consumers is a high priority for us.

1.2 These consumers often have unpredictable variations in their income and expenses. They are generally higher risk and borrow smaller sums than consumers of mainstream credit. As a result, their cost of borrowing is normally higher. This increases their overall financial burden and could put them at risk of defaulting on other payments, such as rents and bills, and getting further into debt.

1.3 We launched the high-cost credit review in November 2016 to identify patterns and sources of harm to consumers across high-cost credit products, and identify whether specific products or types of credit needed deeper investigation.

1.4 As part of this work we reviewed the price cap on high-cost short-term credit (HCSTC – commonly referred to as pay day lending) that we introduced in January 2015. We set out our findings on the impact of the cap in our July 2017 Feedback Statement.[1] We found that the cap, together with the other regulatory changes we introduced, had improved outcomes for consumers. We therefore decided to maintain the cap at its current level for a further three years.

1.5 We identified overdrafts (arranged and unarranged), rent-to-own (RTO), home-collected credit and catalogue credit as areas for further review. We have also included store cards, given their many similarities with catalogue credit products.

1.6 This paper explains our proposals for new rules and guidance to reduce consumer harm on RTO, home-collected credit, catalogue credit and store cards. Our proposals are designed to give users of high cost credit greater control and protection. We also explain our plans for further work assessing potential rules to introduce a price cap on RTO goods, and the level and structure of a possible cap.

1.7 We discuss our work on overdrafts in a separate consultation and discussion paper published today (31 May 2018).[2]

1 https://www.fca.org.uk/publications/feedback-statements/fs17-2-high-cost-credit
2 FCA CP18/13 (2018) HCCR publication, https://www.fca.org.uk/publication/consultation/cp18-13.pdf

Who this applies to

1.8 The following firms and organisations should read this document:

- rent-to-own firms and firms offering hire purchase and conditional sale (Chapter 2)
- home-collected credit firms (Chapter 3)
- catalogue credit firms and store card providers (Chapter 4)
- consumer bodies and stakeholders interested in helping consumers and firms looking to provide low or 'mid-cost' credit-related services to consumers of high-cost credit, for example credit unions and community development finance institutions (CDFIs) (in particular, Chapter 5)
- anyone interested in helping consumers get essential household goods, in particular registered social landlords (Chapter 5)

1.9 This CP will also be of interest to other credit firms, trade bodies and consumer organisations.

The wider context of this consultation

1.10 We have been tackling issues in the high-cost credit markets since we took over regulation of consumer credit in 2014. Our interventions so far have resulted in a transformation of some high-cost sectors. We have taken significant action where firms fail to meet our standards, using the authorisations process, supervisory work and, where appropriate, enforcement. Firms have made substantial improvements, particularly in their creditworthiness assessments and dealing with consumers in financial difficulty. By February this year, we had secured a total of £901 million redress (write downs and payments) for more than 1.7 million consumers where consumer credit firms had fallen short of our expectations.

1.11 Our cap on HCSTC and measures such as restrictions on the use of rollovers have resulted in consumers paying less, repaying on time more frequently and being less likely to need help with problem HCSTC debts. The changes have also helped to protect consumers who should not have been getting HCSTC.

1.12 In the mainstream credit markets, our Credit Card Market Study found that competition was working fairly well for most of the 30 million consumers who have a credit card (60% of the adult population). However, we had significant concerns about the scale, extent and nature of problem credit card debt and firms' limited incentives to reduce this. In February, we published final rules and guidance requiring firms to help consumers in persistent credit card debt and to intervene earlier, using the data available to them to identify consumers at risk of financial difficulties and to then take appropriate steps. These new rules are part of a package of measures to reduce the number of customers with problem credit card debt and to put consumers in greater control of their borrowing.[3]

3 https://www.fca.org.uk/publications/policy-statements/ps18-04-credit-card-market-study

1.13 In July 2017 we published our Feedback Statement (FS) on the main issues we identified in our review of high-cost credit. We set out our decision to retain the cap on HCSTC at its current level for a further three years. We also published a detailed analysis of patterns of use for high-cost credit products. This identified a number of issues which could cause consumer harm, in particular, rent-to-own, home-collected credit and catalogue credit and overdrafts, both arranged and unarranged. We have also included store cards in the review, given their similarities with catalogue credit. Our proposals for overdrafts are set out in an accompanying paper.[4]

1.14 We have gathered evidence to get a deeper understanding of the distinct features and problems of these products. We have analysed the harm and the causes of that harm, and have designed a set of proposals which we believe most effectively tackle the harm. The causes of the harm are different for each product, and the remedies we propose are different in each case.

1.15 During this work, we have taken into account that the reasons people use high-cost credit products reflect a broad and complex set of issues. In particular, that demand for some high-cost credit products is increased by the lack of alternatives to high-cost credit, and little awareness of the alternatives that do exist.

1.16 Throughout this review we have considered where we can work with others to influence developments, in particular to address barriers to the development of lower-cost alternatives. We also make a number of recommendations to Government.

Proposals and issues for discussion

1.17 Our proposals aim to reduce costs to consumers, improve sales practices, protect consumers at risk of financial difficulty, ensure repeat borrowing is consumer-led and encourage market innovation to make alternatives more widely available. This paper is structured as follows:

- Chapter 2 sets out a discussion on RTO pricing and we ask for views to inform our further work on assessing a price cap for RTO. It also sets out for consultation a proposed ban on the sale of warranties at the point of sale.
- Chapter 3 sets out proposals for consultation for home-collected credit.
- Chapter 4 sets out the measures we are consulting on for catalogue credit and for store cards.
- Chapter 5 discusses the steps we are taking to promote alternatives to high-cost credit.

Rent-to-own

1.18 The costs to consumers of using RTO are high, sometimes exceptionally so, both when compared with what consumers would pay on the high street for the underlying goods and when compared against the cost of using other forms of high-cost credit to borrow the money to finance the purchase.

4 FCA CP18/13 (2018) HCCR publication, https://www.fca.org.uk/publication/consultation/cp18-13.pdf

1.19 Given the issues we have identified with RTO pricing, we believe the case is made, in principle, to consider the introduction of a price cap. We believe that the costs of RTO and the financial vulnerability of the consumers who use it provide sufficient grounds for us to undertake the significant additional analysis we need to reach a final conclusion on consulting on the structure, level and rules for a price-cap.

1.20 Under the Financial Services and Markets Act 2000 (FSMA), we are required to formally consult on rules we propose to introduce. Consultations must be open and transparent, and the FCA cannot prejudge the result. In order to consult, the FCA must have a sufficient evidence base on which to base its proposals and develop a cost-benefit analysis. These checks and balances ensure any proposed measures are proportionate and necessary to protect consumers.

1.21 Whilst we undertake that work, we remain open-minded to alternative solutions that could protect consumers from the harm associated with these high costs. We welcome views from stakeholders on what these alternative solutions could be.

1.22 In addition, there is action we can take now on one aspect of the costs. We are consulting on new rules to ban the sale of extended warranties alongside RTO agreements at point of sale. We believe extended warranties are of limited value to consumers when similar cover is provided by standard manufacturers' warranties. Our proposal will help consumers to decide if they want to buy this product.

Home-collected credit

1.23 In home-collected credit we have identified particular risks to consumers of repeat borrowing and long-term use of what is essentially a shorter-term product.

1.24 We are proposing new rules to ensure firms are treating customers fairly when they borrow again. We have also observed consumers re-borrowing in ways which add to the already high costs of borrowing.

1.25 We are consulting on guidance setting out our view on the interpretation of the ban on 'canvassing' cash loans off trade premises in the Consumer Credit Act 1974 (CCA). This makes clear that firms cannot visit a customer to offer new loans or refinancing unless this is in response to a specific request by the customer. This will help ensure firms do not unduly influence consumers to borrow again.

1.26 We are also consulting on a new rule that means firms will have to provide consumers the comparative costs of taking out another loan on top of an existing loan, so they can compare with the costs of refinancing (which may be more expensive overall).

Catalogue credit and store cards

1.27 For catalogue credit and store cards, we have identified similar concerns to those that we have previously addressed for credit cards. These include whether consumers understand these complex products, and what fees and charges they might incur and when. We have also identified harm associated with a lack of control over credit limit increases, and a lack of protection for consumers at risk of financial difficulties and problems of persistent debt.

1.28 We have also widened our focus to include store cards. While store card consumers tend to have higher credit scores on average than those using catalogue credit, the products share many similarities.

1.29 We are consulting on new rules to:

- Require catalogue credit and store card firms which offer 'buy now pay later' (BNPL) and similar offers to provide consumers with clearer explanations of the implications and costs of not paying back within the offer period.
- Require these firms to remind their customers when the offer period is about to come to an end to prompt repayment.
- Give catalogue credit consumers more choice about whether and how their credit limits are increased.
- Ensure catalogue credit firms do not give credit limit increases to customers in financial difficulties or increase the interest rate on their account.
- Require firms to use the information they hold to identify customers at risk of financial difficulty and take appropriate steps. We also propose to apply these rules to store cards.
- Require firms to offer customers in persistent debt help to repay it more quickly. We also propose to apply these rules to store cards.

Alternative forms of credit

1.30 Aside from addressing specific issues identified with particular forms of credit, we also considered wider issues in the sector. In particular, we have considered the degree to which demand in the RTO market may partly be driven by the social housing system and by the lack of availability or awareness of alternatives to high-cost credit. In this regard, we were struck by the relatively low availability of "mid-cost" credit.

1.31 To address these issues a number of public authorities will need to work together. Areas we think are particularly promising are:

- The role of local authorities and registered social landlords (RSLs) as direct providers of furniture and household goods, or as introducers (brokers) for others who may offer alternative sources of credit.
- The development of credit unions or CDFIs as alternative lenders. We can observe some interesting partnerships here and are encouraging innovative ideas via our own Sandbox programme.
- Capital is vital here – the Government's commitment of £55m in dormant assets is a good start, but we think there is more to explore to encourage commercially viable "mid-cost" lending.

1.32 In the immediate term, we propose to consult on guidance to make it as simple as possible for social landlords to offer their tenants information about where to obtain credit if they need it. If RSLs require FCA authorisation, we have established a dedicated team to assist them.

1.33 We also consider there is a case for the Government to contemplate changes. One area for possible change is in the guidance to social landlords on the Universal Credit Regulations 2013 to clarify how furniture schemes can operate under the universal credit system. A second area is whether the exemptions for local authorities under

FSMA for credit broking should be extended to RSLs through a change to the regulated activities order, increasing the scope for RSLs to help their tenants understand the options available outside RTO.

Outcomes we are seeking

1.34 We expect this proposed package of measures to reduce harm and improve outcomes for consumers in the following ways:

- Subject to our further evidence gathering, reduce the harm from RTO pricing.
- Consumers will choose which high-cost credit products to use with a better understanding of what might be available to them, reducing the extent to which they believe that they have no other options.
- Organisations, such as RSLs, will help consumers understand their options at points in time when they may be particularly susceptible to harm from high-cost credit.
- Consumers will be helped to use the credit products they take out in the way they were designed, for example with protections to prevent consumers holding long-term debt on products that are designed for short-term use. This will reduce the incidence of charges that consumers face.
- The changes we are proposing will also give consumers greater control over the amount of credit they take on, for example through rejecting credit limit increases and only discussing further home-collected credit borrowing if they want to. This will help prevent consumers taking on more debt then they want, and reduce the risks of financial distress.

1.35 In considering the outcomes, we will take into consideration the benefits to consumers from having access to credit from both commercial and non-profit organisations.

Equality and diversity considerations

1.36 We have considered the equality and diversity issues that may arise from the proposals in this Consultation Paper. We consider this further in Annex 4 in our Equality Impact Assessment.

1.37 Our initial assessment has found that our proposals do not result in direct discrimination for any groups with protected characteristics. We have identified that groups with protected characteristics make up the majority of home-collected credit and rent-to-own consumers; however we consider our proposals will have a positive impact on consumers and groups with protected characteristics.

1.38 We will continue to consider the equality and diversity implications of the proposals during the consultation period, and will revisit them when making the final rules. In the meantime we welcome input to this consultation on this.

Measuring success

1.39 We will develop metrics to assess the success of any final rules we make. For example, we may expect to see:

- fewer people in persistent debt with products not designed for longer-term debt
- increased awareness of the benefits of, and satisfaction with, extended warranties for those that elect to buy them
- greater understanding of the products, indicated by, for example, a reduction in the proportion of consumers missing repayment deadlines for buy-now-pay-later offers

Next steps

1.40 We are starting our detailed work on considering a potential price cap in the RTO market immediately. Please reply to the discussion elements of this paper by 13 July.

1.41 If we conclude that a price cap and associated rules are warranted, we would expect to consult on draft rules in Autumn this year and for the rules to be in force by 1 April 2019 (this timing is subject to the outcome of the additional work we need to undertake).

1.42 Please respond to the consultation questions in this paper by 31 August to cp18-12@fca.org.uk. Subject to the responses to consultation that we receive, we aim to finalise these rules in Autumn and for the rules to come into force early in 2019.

2 Rent-to-own

Summary

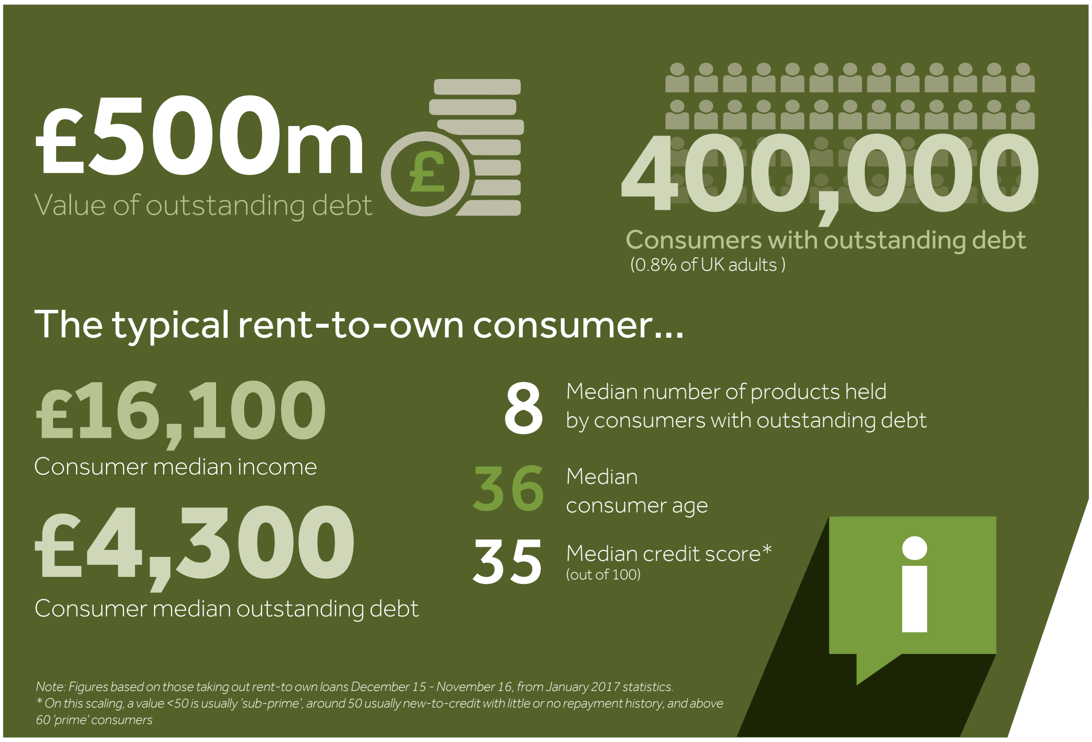
2.1 RTO retailers offer household items, such as washing machines and televisions, in-store and online, with consumers making weekly payments. Consumers hire the goods for a period (usually three years) under a hire-purchase agreement. They can then choose to take over ownership of the goods when they have made all the payments.

2.2 In this chapter we set out our findings on the RTO sector. We also explain our next steps for addressing the harm to consumers of the very high costs of using RTO. Consumers often pay many times what they would pay from a high-street retailer and even two to three times what they would pay if they used other forms of high cost credit. This suggests a significant market failure that affects vulnerable consumers.

2.3 When we took on regulation of the consumer credit sector in 2014, we were given an express power to make general rules about the cost of credit. This provides, among other things, that we have the power to cap charges for regulated credit agreements. In the specific case of HCSTC, Parliament placed an obligation on us to make rules using this power with a view to securing an appropriate degree of protection for borrowers of HCSTC against excessive charges.

2.4 If we conclude that it is appropriate to do so in the light of responses to this discussion paper and further analysis, we would consult on a proposal to use these powers in relation to the cost of credit in the RTO market.

Consumers using RTO[5]



Background

2.5 RTO is a relatively small market of around 400,000 consumers, but many of them are potentially vulnerable. RTO consumers are typically in difficult circumstances and are on average becoming increasingly indebted. In 2016 they had a median income of £16,100 and our consumer research indicates that some users rely to some extent on state benefits for income, such as disability living allowance, which can limit their options for getting credit.[6]

2.6 Our calculations take into account all the debt that is held by these consumers and recorded on credit reference files. They show the median amount of their outstanding debt more than doubled from £2,000 in November 2014 to £4,300 in November 2016.

Findings

2.7 We have assessed the extent to which consumers pay more for these goods than those able to pay with cash, through retail finance or by using other high-cost loans to finance cash purchases.

2.8 We collected and analysed a range of data on pricing in the RTO sector, including:

- desk research on pricing, using a range of contract lengths and looking at both weekly and total costs
- a data request to firms, focusing on pricing policies, features, take-up and the rates of consumers making claims against extended warranties

5 Feedback Statement: High-cost credit including review of the HCSTC price-cap, FCA, July 2017 https://www.fca.org.uk/publication/feedback/fs17-02.pdf
6 FCA analysis of credit reference agency data as published in FS 17/2

- consumer research into consumers' experiences of RTO, perceptions of price and any impacts using RTO has had on their finances
- credit reference agency (CRA) data analysis on RTO users and their total debts

2.9 The overall cost of using RTO potentially has four main components: the cash or base price of goods, the cost of credit, insurance and warranties.

Base price: This is the ticket price of the products sold by RTO firms, which is typically higher than other retailers charge. Few, if any products are sold for cash at this price. It represents the price at which the firm would sell the goods for cash if someone wished to purchase them outright, and is the amount of credit provided to the consumer and is used as a starting point for calculating add-on costs.

Credit: Goods are typically offered at 69.9% APR with some electrical items priced at 99.9% APR. Some firms may vary prices according to risk. APR is, however, a poor indicator of cost here because of the inflation of the RTO base prices.

Insurance: Firms require consumers to hold a valid insurance policy to cover the risk of theft and accidental damage (TAD). Our authorisations work with the sector has led to firms 'unbundling' insurance and offering it as an optional purchase, as consumers may be covered by their own home contents insurance or could get alternative cover. We understand that around 90% of consumers still choose to purchase TAD cover from RTO firms, which has some features which may be beneficial for consumers using RTO (eg no excess charges in the event of a claim).

Warranties: Extended warranties are also sold as an optional extra alongside the agreement. Most goods are covered by a manufacturer's warranty for at least the first year, but the extended warranty can give consumers extra benefits such as faster repairs and a replacement during repairs. There is also no charge incurred should the firm not find a fault with the goods, unlike with a manufacturer's warranty. We understand that around 70% of consumers decide to purchase these extended warranties.

2.10 In assessing pricing in RTO we have considered a number of factors. These include:

- the costs of using RTO vs. other retail options
- behavioural biases we see in consumers' behaviour
- evidence on the alternatives that are available and used by RTO customers
- benefits to consumers of access to RTO against the costs

Costs of using RTO

2.11 We examined a large sample of RTO pricing to establish what consumers pay and how the various pricing components contribute to the overall costs. We used online price comparison information to find out what consumers would pay if they were able to buy goods outright from mainstream high street or online retailers. We largely made comparisons where goods on sale were identical, but where goods were sold on an exclusive basis (eg furniture, which is a significant portion of RTO sales) we also looked at similar products. We looked at the longer term agreements available for each product as most consumers pay over a longer term.[7]

2.12 We set out some examples from this price comparison work in Table 2.1 below and include four different comparisons:

- Column 'A' shows a comparison between the cash price RTO firms charge for the goods and typical high street prices. The comparisons we draw are not from the cheapest available high street/online alternative, but a typical retail price at the time we made the comparison.[8]
- Column 'B' shows the total amount payable by the consumer after interest is added compared with the RTO cash price.
- Column 'C' shows a comparison between the total cost to the consumer, including credit cost, compared with the typical retail price of the goods.
- Column 'D' shows the total cost to the consumer if they bought add-ons with the product (which most consumers take) compared with the typical retail price of the goods. However, this assumes that consumers buying goods through mainstream retailers do not take out additional insurance or warranties, for which there would also be additional cost.

Table 2.1: RTO pricing compared with mainstream high-street alternatives

Product (3 year term unless specified)	Typical Retail Price	RTO Cash Price	RTO Total Cost w/credit	RTO total cost w/add-ons	A – RTO cash price vs Typical high Street price	B – RTO price plus interest vs RTO cash price	C – RTO price plus interest vs Typical high street price	D – RTO total cost incl interest and add-ons vs Typical high street price
Indesit 50cm Electric Cooker (Installed)	£300	£522	£1,044	£1,576	1.7	2.0	3.5	5.3
Sony Xperia XA1 – White (2 years)	£200	£354	£650	£883	1.8	1.8	3.3	4.4
Indesit 6+5KG Washer Dryer (Installed)	£320	£584	£1,168	£1,551	1.8	2.0	3.7	4.9

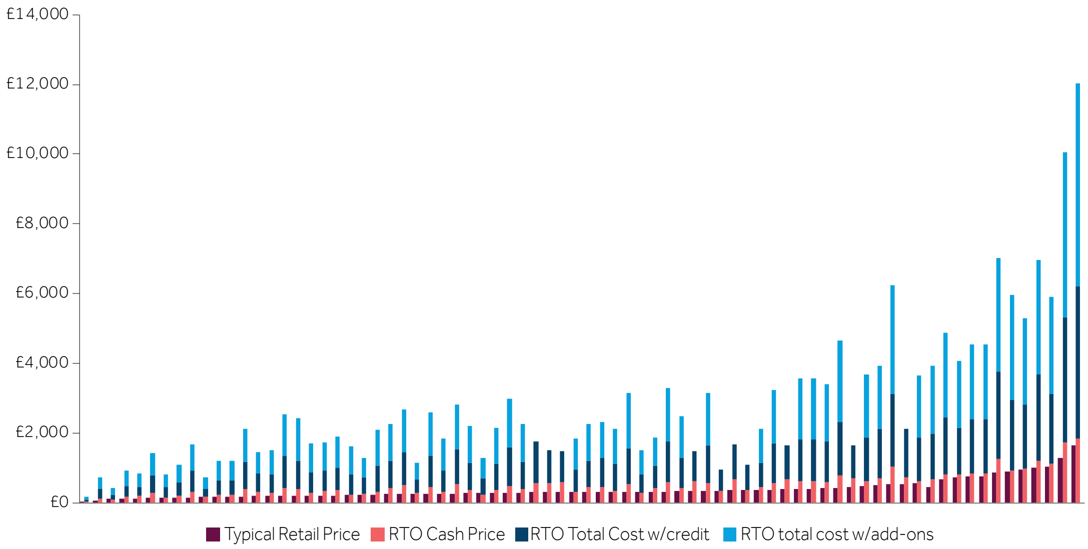
7 We found that approximately 55% of RTO agreements 2014-2018 were longer than two years in duration.

8 For this figure and columns B-D we have given the higher cost as a multiple of the lower cost. ie Column A for the first example shows that the cash price charged by RTO firms is 1.7 times more expensive than the typical high-street price. Column B shows that the finance charges double the RTO cash price. Column C shows the combined effect: that an RTO consumer would pay 3.5 times the typical retail price. And Column D shows that if consumers purchased the insurance and warranties, they would pay 5.3 times the typical retail price.

Product (3 year term unless specified)	Typical Retail Price	RTO Cash Price	RTO Total Cost w/credit	RTO total cost w/add-ons	A – RTO cash price vs Typical high Street price	B – RTO price plus interest vs RTO cash price	C – RTO price plus interest vs Typical high street price	D – RTO total cost incl interest and add-ons vs Typical high street price
"Harper" 2 Seater Fabric Sofa vs. Harveys 2 seater fabric sofa	£290	£490	£1,092	£1,415	1.7	2.2	3.8	4.9
Apple iPhone SE 32 GB (78 weeks)	£300	£464	£741	£1,065	1.5	1.6	2.5	3.5
Hoover Slimline Dishwasher	£240	£318	£741	£1,028	1.3	2.3	3.1	4.3
Hotpoint 60cm Gas Cooker (Installed)	£540	£1,044	£2,089	£3,112	1.9	2.0	3.9	5.8
Sony Shake X30D Home Audio System	£550	£618	£1,248	£1,795	1.1	2.0	2.3	3.3
BOSE Bluetooth Headphones (2 years)	£300	£456	£821	£1,036	1.5	1.8	2.8	3.5
Acer One 10 Notebook Laptop (2 years)	£245	£425	£780	£1,068	1.7	1.8	3.1	4.3
Average (selected examples shown here)	**£329**	**£528**	**£1,023**	**£1,453**	**1.6**	**2.0**	**3.2**	**4.4**
Average (all 75 examples)	**£400**	**£544**	**£1,045**	**£1,444**	**1.5**	**1.9**	**2.7**	**3.7**

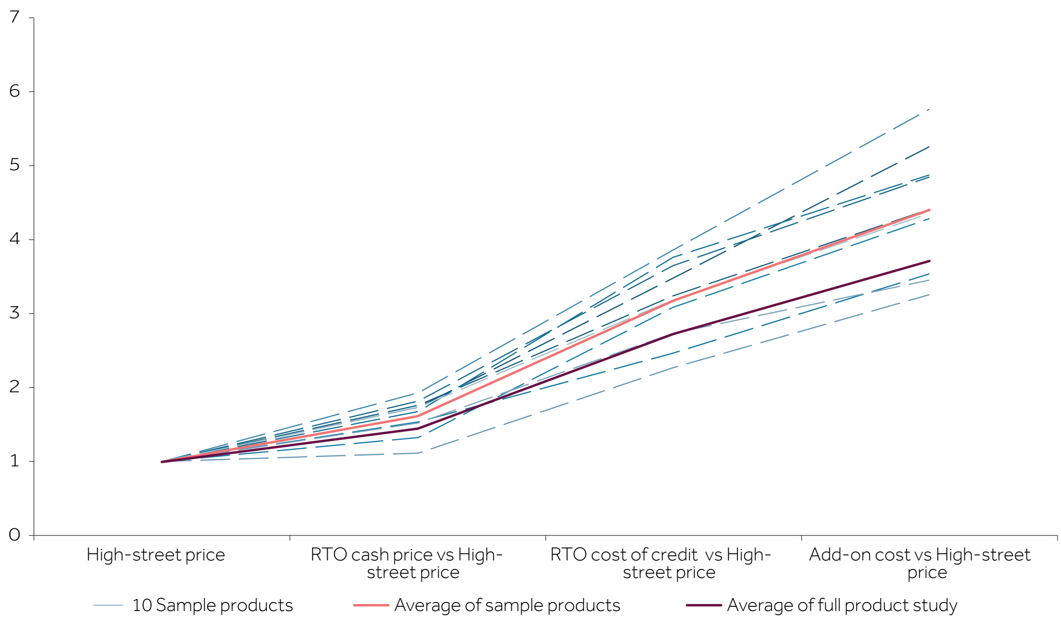
2.13 Figure 2.1 demonstrates how the components of RTO pricing combine to increase the costs paid by consumers. Each column represents a product from our sample, shown alongside the typical retail price for the goods.

Figure 2.1: Retail price compared with potential prices paid by RTO consumers



2.14 Figure 2.2 shows the price comparisons included in Table 2.1. above for the ten products in the sample and the average across the full sample.

Figure 2.2: RTO costs shown indexed against high-street pricing



2.15 Our analysis confirmed that the cash price of goods from RTO firms is typically higher than the cash prices for identical or similar products available at other retailers, often significantly so. The cash prices quoted by RTO firms were on average 45% more expensive than high-street equivalents. The extent to which the cash price is more than other retailers has a major impact on the total cost as consumers pay interest on this higher price. However, we also found some examples where RTO firms offer some goods at the same price or even less than some high street retailers, though this was rare (4 of 75 examples).

2.16 For the full sample in our analysis of pricing we found that using RTO without add-ons but inclusive of the cost of credit was on average 2.7 times more expensive than buying goods outright from the high-street or online. This ranged quite significantly from

1.1 times more to 4.7 times more. For agreements with term lengths of three years or longer (approximately half of all RTO agreements) consumers would pay three times as much as buying without credit at mainstream high street and online retailers on average.

2.17 We have looked at the impact of purchasing add-ons from RTO providers across the product term. This is relevant because approximately 90% of consumers buy TAD insurance and 70% buy extended warranties. We have found that these significantly add to the price consumers pay. Firms have reported that the majority of consumers buy both TAD insurance and extended warranties.

2.18 We found that on average using RTO with add-ons is 3.7 times more expensive than buying outright elsewhere, sometimes as much as 5-6 times more expensive. However, a raw comparison of the total costs of using RTO, including these add-ons and the high-street prices consumers pay, does not reflect the value consumers get from protection against theft and accidental damage or for repairs given under extended warranties.

2.19 We have also compared the costs of using RTO with home-collected credit, which we have found to be the nearest available alternative for many consumers (Table 2.2). We found that in many cases taking out a standard 52 week loan (which is generally the longest term loan available to new customers) would lead to significant savings against using RTO, often up to half. Although this is likely to include higher weekly repayments which may affect consumers' preferences or ability to pay. We also recognise that there may be other factors which determine consumer preferences for different types of credit.

Table 2.2: RTO pricing compared with home-collected credit

Product (3 year term unless specified)	Typical Retail Price	RTO Total Cost w/ credit	RTO total cost w/ add-ons	RTO Weekly Repayment	RTO Weekly Repayment (w/add-ons)	Home-collected credit equivalent (nearest £50, over 52 weeks)
Indesit 50cm Electric Cooker	£300	£1,044	£1,576	£6.69	£10.10	£10.80 p/w £562 total
Sony Xperia XA1 – White (2 years)	£200	£650	£883	£6.25	£8.49	£7.20 p/w £374 total
"Harper" 2 Seater Fabric Sofa vs. Harveys 2 seater fabric sofa	£290	£1.092	£1,415	£7.00	£9.07	£10.80 p/w £562 total
Indesit 6+5KG Washer Dryer (Installed)	£320	£1,168	£1,551	£7.49	£9.94	£12.60 £655 total

Product (3 year term unless specified)	Typical Retail Price	RTO Total Cost w/ credit	RTO total cost w/ add-ons	RTO Weekly Repayment	RTO Weekly Repayment (w/add-ons)	Home-collected credit equivalent (nearest £50, over 52 weeks)
Apple iPhone SE 32 GB (78 weeks)	£300	£741	£1,065	£9.50	£13.66	£10.80 £562 total
Hoover Slimline Dishwasher	£240	£741	£1,028	£4.75	£6.59	£9.00 £468 total
Hotpoint 60cm Gas Cooker (Installed)	£540	£2,089	£3,112	£13.39	£19.95	£19.80 £1,030 total
Sony Shake X30D Home Audio System	£550	£1,248	£1,795	£8	£11.51	£19.80 £1,030 total
BOSE Bluetooth Headphones (2 years)	£300	£821	£1,036	£7.89	£9.96	£10.80 £562 total
Acer One 10 Notebook Laptop (2 years)	£245	£780	£1,068	£7.50	£10.27	£9.00 £468 total

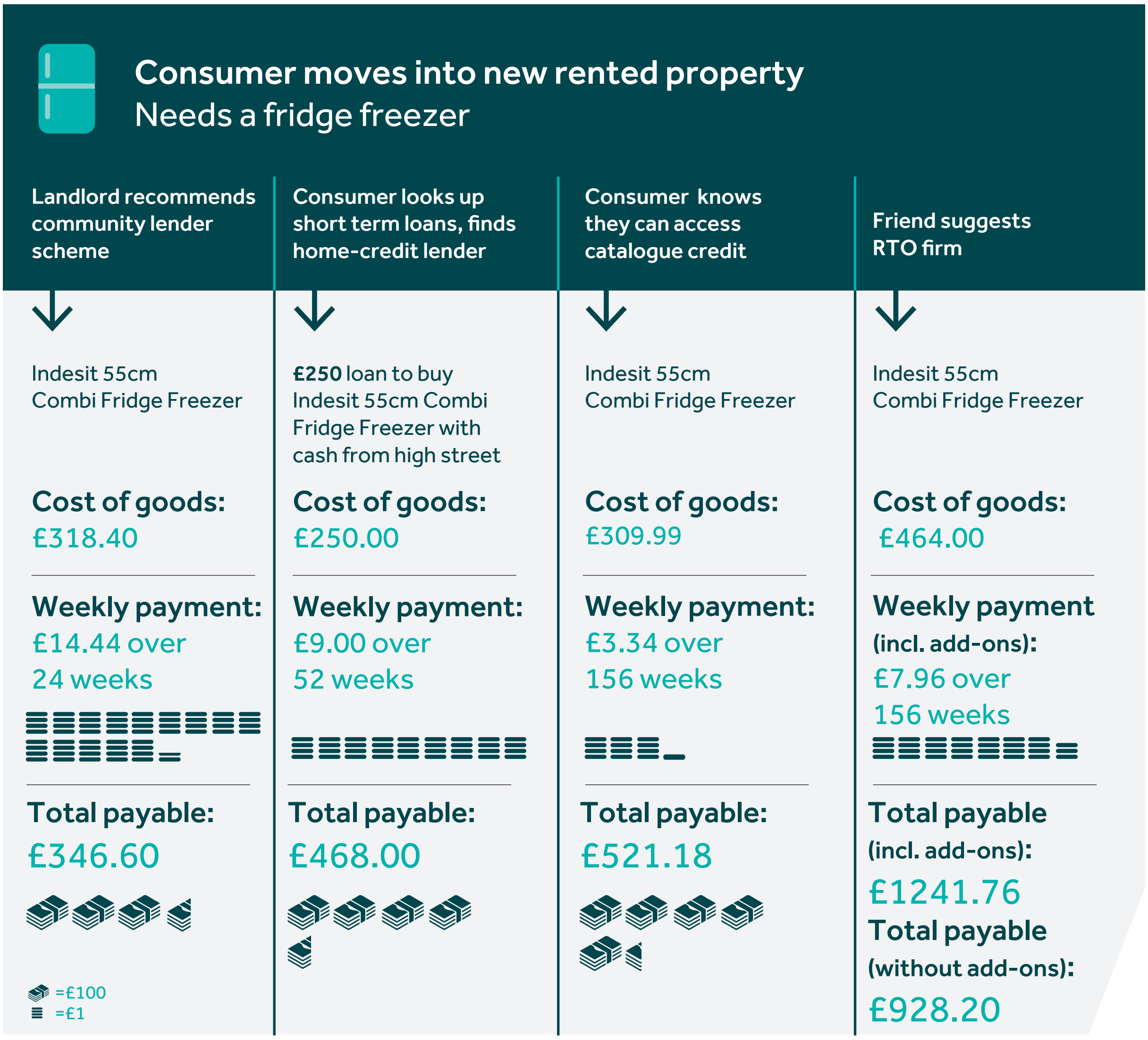
2.20 We also examined options for buying goods on retail finance with add-ons compared with the costs of using RTO, to examine the savings that could be made if consumers were eligible for this type of credit. We set out one example in table 2.3.

Table 2.3: RTO costs compared with retail finance

	Price	Repayment	Price w/ credit	Price w/credit and two year warranty
Samsung Fridge Freezer (RTO)	£588.75	£9.13 per week over 24 months	£949.52	£1,268.80
Samsung Fridge Freezer (Retail Finance)	£404.00	£18.47 per month for 24 months	£478.28	£550.04

2.21 Consumers eligible for catalogue credit may also achieve significant savings compared with RTO and often with lower weekly repayments. We found that a basic cooker costing £6.69 per week and totalling £1,043.64 from a RTO firm could be bought for £3.13 per week totalling £487.55 from a leading catalogue credit firm, a saving of £556.09 over the same period. However, some RTO customers may not be approved for catalogue credit on creditworthiness and affordability grounds.

2.22 None of our comparisons include the cost of contingent charges charged by some RTO firms, catalogue credit firms and other mainstream retail credit providers, for example a £12 charge for a missed payment. As a result the comparisons will be conservative, underestimating the total cost to consumers. No contingent charges are made for home-collected credit.



2.23 RTO firms have set out a number of reasons why the cash prices of goods are higher than those of other retailers, including:

- Low purchasing power due to smaller sales volumes, leading to an inability to obtain best product costs from suppliers due to low volumes and due to sourcing from indirect distributors and wholesalers. These are common issues for smaller retailers, where we do not see similar levels of high pricing.
- Lack of supplier trade credit insurance meaning purchases being made by advance payment.
- Increased operating costs from maintaining a high-street presence and complex retail operation, eg servicing goods, debt collection, and devaluation of goods.

- Increased burden of business rates and other taxes plus the fall in sterling increasing costs of acquisition.
- Costs associated with the flexibility provided to consumers, ie the ability to hand back goods at any time. Many of these goods are then sold as refurbished for a lower cost.

2.24 We have not done a full assessment of whether the costs of providing rent-to-own are reasonably reflected in the price. Whilst cost reflectiveness is informative in considering issues of harm from high prices, it is not central to our considerations on cost, which focus on the consumer.

Reasons for RTO users & behavioural biases

2.25 We commissioned qualitative consumer research to build on our evidence base in understanding consumer use and experience of RTO.[9]

2.26 Consumers using RTO are typically from low income households with a high degree of financial pressure. This includes consumers who are out of work and single parent households with low incomes. Many had poor credit histories, or believed they did, which limited their access to mainstream credit options.

2.27 While some consumers were one-off or irregular users, many relied on high-cost credit to manage their finances week by week and did not believe they would ever get out of debt. RTO users in particular had a perception that RTO fulfilled an immediate need. This was particularly the case in emergency situations, with consumers believing they had limited options but to accept the longer term consequences.

2.28 Some consumers reported positive experiences of using RTO and were happy to continue using these services. For many, visiting a RTO retailer was accepted as being their only means of accessing goods, or 'where you go when you really need it'. This was predominantly driven by ease of access, ease of acceptance and the perceived affordability of weekly repayments.

2.29 However, some consumers said they regretted using RTO and felt the full costs including add-ons only became clear at a late stage in the sales process when they felt it was difficult to change their minds. This reflects the fact that, after a lengthy sales process, consumers have a behavioural bias not to explore alternatives, even when they realise they are going to be paying more than they initially thought. This is partly because of the additional costs of add-ons, but also because some risk-based pricing may be used by firms, meaning some consumers end up paying more than the advertised rates.

2.30 Some consumers we interviewed also said they regretted using RTO when they realised they had already paid a significant sum and were only part way through the term of the agreement. However, most consumers said they would consider using RTO again if their circumstances were the same. Given consumers use, and value, RTO as a method of buying essential and quality-of-life products this is unsurprising.

9 We held a series of 20 interviews with consumers and three focus groups for each high-cost product examined in this paper. See PwC (2018), Usage and experiences of High Cost Credit, https://www.fca.org.uk/publication/research/usage-and-experiences-of-high-cost-credit-consumer-research-report.pdf

Alternatives available to consumers

2.31 In assessing RTO pricing we have considered the alternative options available to consumers. We recognise that RTO firms provide a means for consumers to get household and essential goods at affordable weekly prices. We also know that these consumers have a median credit score of 35, which is among the lowest of all high-cost credit consumer segments. Some consumers reported having had earlier difficulties with indebtedness at a younger age which limited their options at present.

2.32 This may prevent them from accessing retail finance and credit cards, which are typically cheaper and which many people use to fund purchases of household goods. Our consumer research highlighted that many mainstream retailers offering credit will not lend to consumers if they are working less than 16 hours a week or have a household income below a certain threshold, which would exclude some RTO users. A common theme from our interviews with consumers was that they had, or believed they had, a lack of options.

2.33 Most consumers were aware of the costs of using RTO, but did not compare this to other forms of credit. This was particularly true of those that shop in-store, where they felt they were influenced by the in-store environment and the immediacy and tangibility of using RTO to buy goods.

2.34 Our CRA data analysis indicates that 52% of consumers using RTO as of November 2016 also held home-collected credit debts, and 46% held catalogue credit debts. This indicates that some consumers have access to alternative credit options to finance the purchase of goods. Our analysis of credit reference agency data and our consumer research also found a clear demographic overlap between consumers using RTO and home-collected credit, with many participants having once been or currently using both types of credit.

2.35 Our consumer research found that the emphasis of pricing at point of sale is on weekly costs, which consumers respond to and focus on in order to manage their weekly budgets. It appeared that most consumers were aware that RTO is overall an expensive way to acquire goods but, at the time of purchase, they felt their options were limited.

2.36 We recognise that consumers could save significantly from buying goods second-hand. But our consumer research showed that peace of mind was important, particularly for consumers with dependents, and that they were concerned about the longevity or reliability of second hand goods. Some consumers also did not have sufficient savings to buy second hand goods with cash.

Benefits to consumers of using RTO

2.37 Consumers purchase a range of products using RTO. Around 40% of RTO sales are for household appliances and furniture, while the remaining 60% are electrical goods. It is very difficult to define what an 'essential' household item is. For example in a household with school-age children it is the norm to have access to a computer. However, it is reasonable to assume that a significant proportion of sales could be for items that are essential to consumers.

2.38 RTO also has a number of features which are helpful for consumers. For instance, consumers can generally hand goods back at any time without further liability, or upgrade to a new product if they want to[10] (although they would lose their equity in the product if they do this). We collected data from firms on returns and found that in returns are relatively common. In evidence to the House of Lords, the CEO of Brighthouse stated that 'Typically, across all the contracts, about half get to the point of ownership. Maybe a third get to the point where they change their mind at some point in the contract and they hand the product back to us.'[11] Firms argue this is not a reflection of consumers coming into payment difficulties and no longer being able to afford repayments, but using the benefits and flexibility under the RTO agreement which often exceed consumers' statutory rights.

2.39 Consumers choosing to buy goods outright or on retail finance would not have the same flexibility to return or upgrade goods. We accept that these benefits are reflected in the pricing to some extent, as firms offer discounts on refurbished and previously used goods so will make a loss when goods are handed back.

For Discussion: Action on RTO pricing

2.40 Our findings make clear that the costs of RTO are high, sometimes exceptionally so. RTO users are paying an average premium of 3 or 4 times the typical retail price of goods. At the extreme, this can be nearly 5 or 6 times. Significantly, RTO is also an outlier compared with home-collected credit which large proportions of RTO customers also use.[12]

2.41 RTO consumers are typically in difficult and deteriorating financial circumstances.[13] Weekly repayments are kept low and spread over a long term in order to make them affordable or to suit those who budget weekly. But affordability of weekly repayments must be balanced with the potential for the overall cost burden to harm the consumer.

2.42 We think it is highly likely that harm is being incurred through both the high levels of charges and the likelihood that a group of consumers would have improved economic welfare if they were denied access to RTO. For these consumers, the benefits of acquiring items through RTO are likely to be outweighed by the significant costs. We think that some consumers would benefit from moving to other, cheaper credit sources or reconsidering their needs and foregoing purchases. Others may benefit from continuing to access RTO at a reduced price. We anticipate that a price cap at the appropriate level may achieve the right balance between avoiding indebtedness for some and continued access to RTO at a lower cost for others.

2.43 Collecting and analysing all of the evidence needed to show whether this would be the case is a major task. We are starting this work now and asking for views on the issues that we should take into account.

Other potential remedies to address high costs

2.44 We have considered a range of other less intrusive remedies to address these issues.

10 Under the Consumer Credit Act consumers are entitled to voluntarily terminate the agreement where they have paid 50% of the total amount payable. The option to return RTO goods at any time is offered in addition to the consumer's statutory rights under the CCA to return goods if they have paid, or pay up to, half of the total amount payable.

11 http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/household-finances-income-saving-and-debt/oral/79773.html

12 Of consumers entering into a rent-to-own agreement Dec 2015 to Nov 2016, 52% also had home-collected credit.

13 p.27 'High-cost credit including review of the HCSTC price-cap: Feedback Statement' ; July 2017, FCA https://www.fca.org.uk/publication/feedback/fs17-02.pdf

2.45 We have examined whether disclosure-based remedies, such as risk warnings or making the information firms give consumers at the point of sale more relevant, could address our concerns about consumer harm from high prices. There are a number of reasons why we think these would not be enough.

2.46 Our supervisory and authorisations work has already helped to improve the transparency of information available to consumers. The information firms currently give to consumers sets out the total costs over the lifetime of the agreement.

2.47 In addition, consumers' focus on weekly costs and on getting the goods limits the impact that information or warnings about the total costs of RTO might have. Our research shows that consumers know that RTO is expensive, but their actual or perceived lack of options limits their ability to react to information about the product's total cost. We consider that changes we could make to the clarity and quality of consumer information would only be slight improvements.

2.48 We have identified a particular concern around selling extended warranties at the point of sale which we address below. However, this only addresses one element of the high costs of RTO.

2.49 Another part of the solution lies in addressing the demand for RTO. For example, some consumers start using RTO because they move at relatively short notice into unfurnished social housing. This creates an immediate need for furniture, appliances and other goods. There are some schemes in the UK that provide furniture and white goods to new tenants, but these are the exception and may be difficult for consumers to identify. We discuss our work in encouraging the availability and use of alternative means of obtaining essential goods at Chapter 5 below.

2.50 We hope that our work in this area, in collaboration with others, will help shift the market demand for RTO and address the market failures that in part drive this demand. However, we do not expect these actions to deliver the scale of change required in the near future to benefit the full range of consumers who could be assisted.

2.51 We remain open to suggestions about steps we could take to address the harms we have identified. But in the absence of other effective measures to protect consumers, we believe there are sufficient grounds to undertake the significant additional analysis needed to reach a conclusion on whether to consult on a price cap. We will, therefore, launch the work that is needed to do this.

Developing a price-cap

2.52 Developing proposals for a price cap is a complex and resource intensive task, which will need to make a comprehensive assessment of the impact on consumers and firms covering, for example:

- **The structure of a possible cap** – we would need to consider how to structure a cap, taking into account the specifics of the RTO service and the different components of RTO pricing. This would consider international experience[14] and take into account how easily understood a cap would be for consumers. Creating an appropriate structure for an RTO cap is not simply a question of extending the scope of the cap that we introduced for HCSTC.

14 The Australian government has recently announced it will legislate to impose a price-cap on consumer leases (similar to the UK RTO sector) based on a multiple of the recommended retail price for each whole month of the lease term, inclusive of all add-ons.

- **The impact on consumers** – we would need to assess both the benefits to consumers who continue to use RTO and the implications for those who may no longer be able to use it. This would include a detailed consideration of what consumers who could no longer get RTO would do and whether this would be beneficial for them. This would include further consideration of how to improve the availability of alternatives to high-cost credit and the importance of supporting their development.

- **The impact on firms and the market** – we would model the financial impact of any intervention on pricing, and the impact on the market for RTO and competition in the market.

Questions for Discussion

2.53 We are seeking views at this stage on the issues we should take into account in this assessment.

> **Q1:** **[For Discussion] What alternative solutions could there be to address harm from high prices?**

> **Q2:** **[For Discussion] What issues should we should take into account in carrying out further work on a price-cap?**

For Consultation: Proposal for a point of sale ban on extended warranties

Point of sale ban on extended warranties

2.54 We propose new rules to address one element of the costs to consumers of using rent-to-own before we start our work on a broader intervention on price – these proposals are with regard to extended warranties.

2.55 Extended warranties are an optional extra alongside RTO agreements. They operate in the event that goods are damaged or have faults and may need repairs or replacement. This is separate from TAD insurance, which consumers must have as a condition of the hire-purchase agreement.[15] Warranties are intended to cover product faults which fall outside the TAD insurance.

2.56 Most goods are covered by a manufacturer's warranty for at least the first year of the RTO agreement, at no additional cost to the consumer. Even without an extended warranty, firms currently allow consumers to return goods if they are no longer satisfied, although they lose their equity in the product if they do so. Consumers also have broader rights to return goods under legislation, such as the right to return goods that are not of satisfactory quality, fit for purpose or as described under the Consumer Rights Act 2015.

2.57 Around 70% of consumers decide to purchase extended warranties and the claim rates are reasonably high, with £4 paid out in claims for every £10 taken in premiums. However, we do not know how many of these claims would have been met by the underlying manufacturers' warranty.

15 Consumers may opt to buy this from the RTO provider or elsewhere.

2.58 The cost of extended warranties are added to the RTO repayment and can be significant – typically around 20% of the weekly repayment cost. For example, a fridge freezer would cost approximately £70 extra in the first year when purchasing the extended warranty and £210 over a three year term.

2.59 Extended warranties provide some benefits over standard manufacturers' warranties. These include faster repairs, like-for-like replacements of damaged goods and no fees for call-outs where there is no fault found. Customers who claim on the standard manufacturers' warranty may also have the additional inconvenience of having to deal with the manufacturer directly (although some RTO firms currently service some standard warranties themselves). The extended warranty can be cancelled at any time. Consumers pay for the warranty weekly and are not obliged to pay anything more on cancellation.

2.60 Firms told us that consumers value the peace of mind that comes with having extended warranty cover. Many of the household goods covered by warranties are seen as essentials which consumers need to be able to use continually.

Issues for consumers buying warranties

2.61 Our consumer research found that some consumers are unclear whether add-on products are optional. Consumers were also not able to easily distinguish between TAD insurance, manufacturers' warranties and extended warranties. This indicates that they do not understand the different types of coverage and protection. Some consumers had little knowledge of what each type of cover included, and some who took out their provider's extended warranty did not know their product would also be covered by a manufacturer's warranty.

2.62 This meant that some RTO customers were adding to the cost of their weekly repayments without fully knowing what they were getting for their money. Consumers claimed that the sales people did not explain the differences between different types of product and positioned them as one package. This means that consumers did not necessarily know they could choose to purchase the TAD insurance and not purchase the extended warranties, or vice versa.

2.63 Our previous research on how buying products as add-ons affects decision-making is also relevant. In July 2014 we published our findings from the General Insurance Add-ons Market Study.[16] Findings included that:

- Add-on distribution models affect consumer decision making. Consumers focus on buying the actual goods, leading many to buy add-ons they do not need or understand. They are less likely to shop around, less price sensitive, and lack awareness of whether they have bought add-on products.

- Add-on providers benefit from a clear point of sale advantage, where the value or otherwise of the product does not tend to affect sales.

2.64 We also examined the extensive studies on extended warranties, previously conducted by the Competition Commission and OFT.[17] These found that firms selling warranties alongside domestic electrical goods had a significant point of sale advantage. They also found information asymmetries (imbalances of knowledge about the product)

16 https://www.fca.org.uk/publications/market-studies/general-insurance-add-ons-market-study
17 http://webarchive.nationalarchives.gov.uk/20140402172757/http://oft.gov.uk/shared_oft/markets-work/OFT1403.pdf

between consumers and firms. This led to a new independent website to compare extended warranties.[18]

2.65 For sales of guaranteed asset protection (GAP) insurance we introduced a deferred opt-in and greater information disclosure. The purpose of this measure was to encourage consumers to shop around, and we are currently reviewing its impact in producing positive consumer outcomes.

2.66 Although RTO customers can cancel warranties at any time, our consumer research shows that many consumers exhibit post-sale inertia and are unlikely to do so.

Proposal

2.67 Given the behavioural biases associated with add-on purchases and the evidence from consumers that this is an area they do not fully understand, we are proposing a point of sale ban on extended warranties sold by RTO firms. This will consist of a deferred opt-in and a requirement that customers are given additional information when they are offered the extended warranty. We want consumers to have time to consider whether they need extended warranties, particularly where they are already covered by manufacturers' warranties as standard. They may also wish to consider buying an extended warranty from another provider.

2.68 This will also avoid some of the behavioural biases associated with add-on sales. Firms will be required to do more to explain to consumers the differences between manufacturers' warranties and extended warranties. It is essential that the typically financially vulnerable consumers using RTO can make informed choices about the value they get for the additional costs they will be paying.

2.69 We propose that RTO firms will not be permitted to offer and sell extended warranties on the same day. Instead there would be a deferral period of at least two clear days, starting when the customer is given pre-sale information.

2.70 Consumers would then be able to decide to buy the extended warranty cover from three days after they receive the information as follows:

Day one	Information is provided to the consumer about extended warranties
Day two	Deferral period
Day three	Deferral period
Day four	Extended warranty sale can be concluded

2.71 Firms can choose when the deferral period can begin according to their current sales processes. Firms are able to follow up once the deferral period has ended, including later in the RTO contract before the standard manufacturer's warranty cover expires. As firms are in regular contact with customers to collect payments, they could have a subsequent discussion on warranties after the deferred opt-in without placing any additional burden on their processes. We do not see a material risk of products developing a fault within three days, and would expect firms to handle this through usual cancellation rights under the two week cooling off period.

2.72 We propose that consumers will be able to conclude an extended warranty sale the day after the information is provided to them by the firm – provided this is initiated by the

18 http://www.compareextendedwarranties.co.uk/

consumer, and they confirm they are aware of the deferral period and consent to this being waived.

2.73 The proposed new rule also requires firms to give consumers sufficient, prominent information so they can make an informed choice to buy the extended warranty. This will include:

- price in terms of weekly cost, annual cost and total cost over the length of the RTO agreement
- significant features and benefits, exclusions and limitations
- that it may be possible to purchase extended warranties elsewhere
- how the extended warranty interacts with and compares with the standard warranty and theft and accidental damage insurance
- when the extended warranty sale can be concluded

2.74 The proposed rules apply to all extended warranties sold by RTO firms, including those which are insurance contracts. Firms will need to consider carefully whether they are providing insurance and should consider the FCA's guidance on this matter in PERG. Firms may also wish to take legal advice and, if in doubt, seek individual guidance from the FCA.

2.75 In designing this measure we have had regard to the factors set out in PROD 2 (the Product Intervention and Product Governance Sourcebook), which limit how we can intervene in setting product rules.

2.76 We have considered alternative measures such as making requirements to improve pre-contract information about the differences between manufacturers' warranties and extended warranties. However our consumer research and previous findings on GAP insurance indicates that information alone is not enough to resolve the significant point of sale advantage that firms have.

2.77 We also considered a ban on the sale of warranties where consumers also have standard manufacturers' warranties. However, we recognise that consumers may get some benefit from having an extended warranty. A ban could have negative outcomes such as consumers being without essential goods while repairs are carried out. It may also lead to firms removing some of the non-statutory benefits they currently provide consumers, such as accepting returns of damaged goods and carrying out repairs under standard warranties in-house.

2.78 We propose that the rules come into force three months after publication.

2.79 We have set out in the draft rules the definition 'rent-to-own-agreements'. We propose that this will cover all hire purchase and conditional sale agreements where consumers make payments more often than monthly, excluding motor finance and all lending to business consumers. The intention is to include all RTO firms. We have not identified any additional hire-purchase or conditional sales business which we think would be inadvertently caught, but we would welcome views on this from stakeholders on this point.

Questions for Consultation

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

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

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

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

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

Next steps

2.80 We are starting our detailed work on considering a potential price cap in the RTO market immediately. In order to ensure that we have the opportunity to take your views into account in our considerations, please reply to the discussion elements of this paper (Questions 1 and 2) by 13 July.

2.81 If we conclude that a price cap and associated rules are warranted, we would expect to consult on draft rules in Autumn this year and for the rules to be in force by 1 April 2019 (this timing is subject to the outcome of the additional work we need to undertake).

2.82 Please respond to the consultation questions on our proposal to introduce a point of sale ban on extended warranties by 31 August to cp18-12@fca.org.uk. Subject to the responses to consultation that we receive, we aim to finalise these rules in Autumn and for the rules to come into force early in 2019.

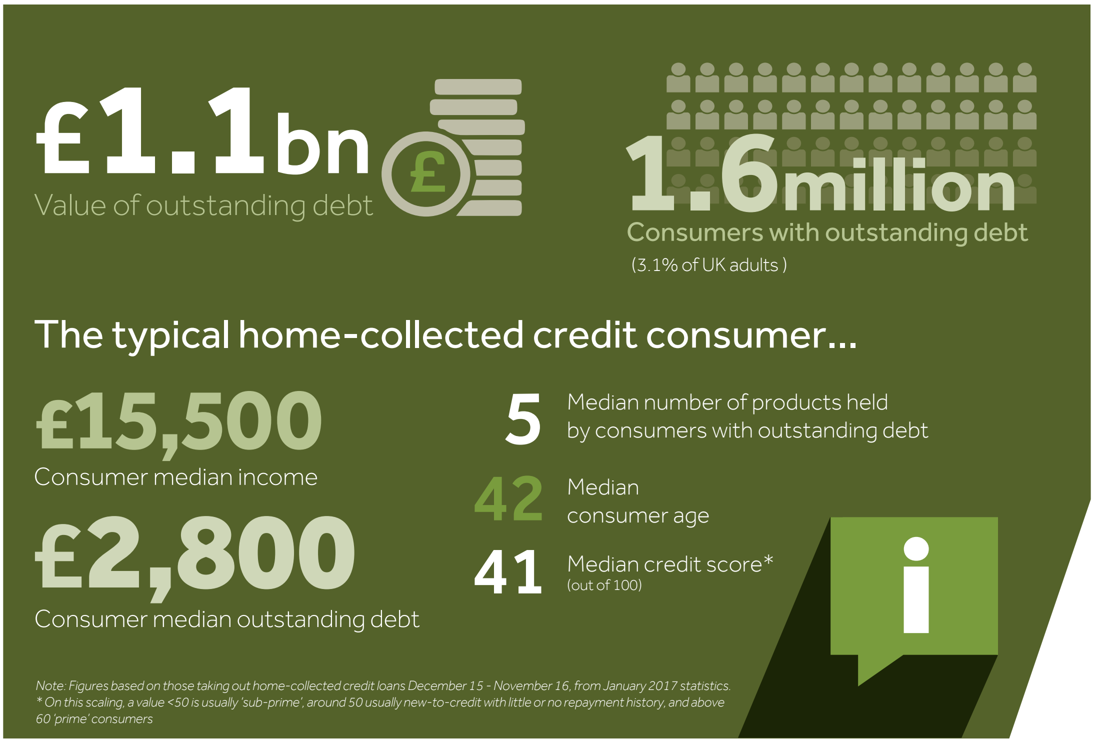
3 Home-collected Credit

Summary

3.1 Home-collected credit involves loans of typically up to £1,000 in cash. Most are repaid in under a year by weekly instalments, which the firms or their representatives collect from the consumers' homes. While home-collected credit is a relatively short-term product, many consumers use it repeatedly and sometimes come to rely on it as an ongoing means of managing an income shortfall.

3.2 In this chapter we set out findings on harm to consumers from longer-term use of home-collected credit and our proposals to address the issues identified.

***Consumers using home-collected credit*[19]**



Background

3.3 We have focused on the risks for consumers of repeat borrowing of home-collected credit, increasing the size of their loans and being in debt over a longer period. We are concerned about the implications of longer term use of home-collected credit, including the additional costs of refinancing when borrowers take out a new loan to pay down part of an outstanding loan.

19 Feedback Statement: High-cost credit including review of the HCSTC price-cap, FCA, July 2017 https://www.fca.org.uk/publication/feedback/fs17-02.pdf

3.4 Generally, consumers are mainly positive about using home-collected credit. Many said that they would be significantly worse-off if this line of credit were unavailable to them. However as with consumers using RTO, there was a common perception that their available options for getting credit were very limited. The fact that loans are arranged and repayments collected in consumers' homes is a valued service, but may also contribute to consumers' potential vulnerability.

3.5 Home-collected credit can be an expensive form of borrowing. For example, a £100 loan over a 52 week period from one leading provider will cost £187.20. There are other providers which are significantly less expensive, with one provider offering a £100 loan over a 51 week term for £140.[20] The absence of charges for missed repayments is a mitigating factor, ensuring that there are no increases in costs even if the consumer takes significantly longer to repay than originally agreed. Our data shows that many consumers miss repayments with around 30% of consumers missing a month's payments according to our most recent CRA data.

3.6 Our concerns centre on the costs of repeated use of home-collected credit rather than the costs of any individual loan. We are therefore not currently planning to develop proposals for a price cap for home-collected credit based on current market conditions. Instead, our proposals directly address the source of harm to consumers from the costs of repeat borrowing and in particular from refinancing.

3.7 A number of comparisons have been made during our study between home-collected credit and HCSTC, with calls to extend the HCSTC price cap to home-collected credit. Such considerations need to take into account the specific characteristics of the particular products and there are significant differences between HCSTC and home-collected credit products. Home-collected credit loans will typically have more, and more frequent, repayments than HCSTC, with few if any contingent charges and no balloon payments at the end of the loan to clear the debt. While the costs for some home-collected credit consumers can accumulate, this is the result of how some firms refinance consumers' loans, rather than the pricing of individual loans. Our proposals aim to address this source of harm directly and we would expect to see reductions in the cumulative cost paid by consumers. We are therefore not currently planning to develop proposals for a price cap for home-collected credit, but will revisit this issue when we assess the effectiveness of the changes we are now proposing.

Findings

3.8 Our consumer research and CRA data analysis has given us further understanding into why consumers refinance and the patterns of longer-term indebtedness in home-collected credit.

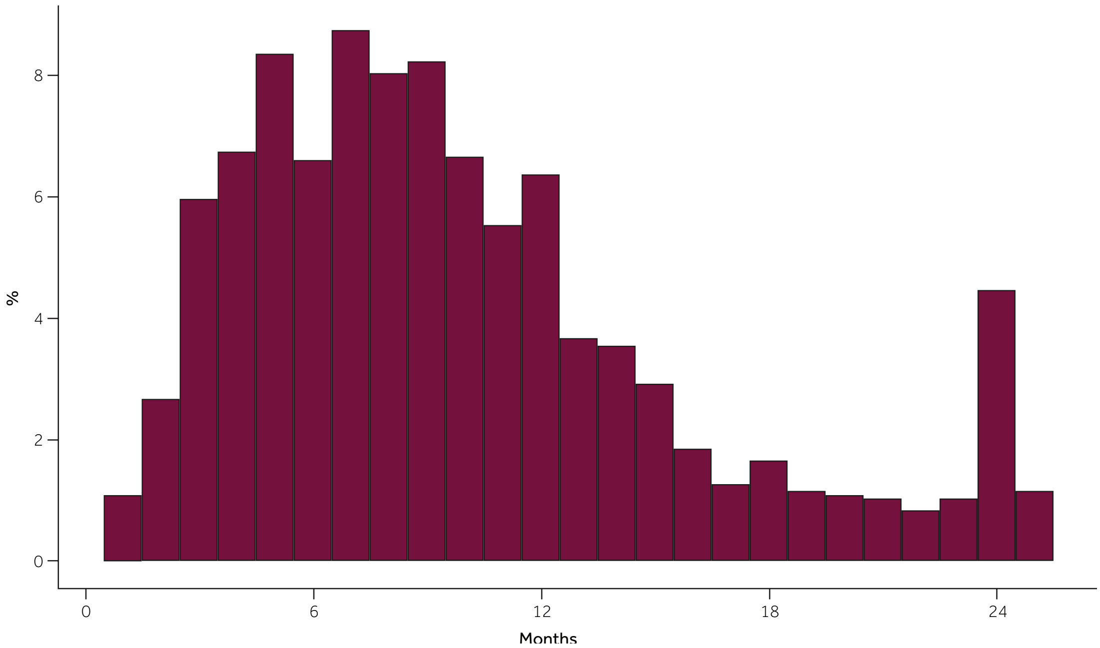
Repeat borrowing and long term use

3.9 Our data indicates that the number of consumers taking out home-collected credit fell from 900,000 in 2012 to 600,000 in 2017. The total value of originations during this period started at £1.4 billion in 2012, falling to £1.1 billion in 2014 and 2015. It rose to £1.3 billion in 2016, but fell back again to £1.1 billion in 2017. Fewer consumers are using home-collected credit, but those that still do are borrowing more.

20 We understand that variations in pricing may be driven, in part, by serving consumer groups with different degrees of risk.

3.10 We have found that repeat borrowing is common in the home-collected credit market. CRA data analysis of a representative set of home-collected credit users from 2015 to 2017 shows that most consumers (74%) spend up to 12 months in continuous debt, and that approximately 5% were in debt for the whole of the two year sample period (Figure 3.1). A majority of consumers (75%) had more than one loan during the period and around 10% had 12 or more loans. Around 50% of consumers had 2 accounts or more in debt at the same time.[21]

Figure 3.1: Duration of debt with home-collected credit products – Most debt spells are between 6 and 12 months



3.11 This is consistent with the data we collected from firms, which suggested that the majority of loans which are refinanced are refinanced once, and nearly 10% of refinanced loans are refinanced three times or more in total.

3.12 Our consumer research indicates that some repeat borrowing is a result of consumers meeting recurring expenditure or occasional emergencies, as many using this form of credit don't have savings. The research identifies two different groups of home-collected credit user. The first is those who imagine they will move away from the product because they expected their personal circumstances to change or whose borrowing was to meet a temporary need, such as car repair. The second is those for whom borrowing has become habitual and is now an entrenched part of their budget.

3.13 Repeat borrowing and multiple borrowing is clearly a prevalent feature of home-collected credit use. We do not consider that this in itself is harmful. Providing creditworthiness assessments are carried out effectively, weekly repayments should be affordable and sustainable. Repeat borrowing can be a useful means of managing cyclical income shortfalls.

3.14 However, we are concerned that there is a small core of customers who are using home-collected credit over an extended period and that some customers are being unduly influenced by firms' representatives to keep borrowing.

21 CRA data analysis of a cohort of consumers who opened home-collected credit accounts in Q3 2017.

3.15 There is evidence from our consumer research that some customers feel firm representatives are quick to suggest that they take out further borrowing when eligible or at certain times of year, such as Christmas or the start of the school year, or simply because they were eligible for additional borrowing because they had repaid a certain percentage of their current loan. Home-collected credit firms are in a privileged position and have the potential to exploit their intimate knowledge of consumers' spending needs. The personal relationships can also be used as a means of subtly influencing consumers.

3.16 In order to mitigate this, we think it is important that requests for borrowing should be initiated by consumers, not firms.

3.17 The existing legal framework already addresses this issue. We are now consulting on guidance to set out our interpretation of the relevant legal provisions. This will be supported by supervision against this interpretation.

Guidance on prohibition on canvassing off trade premises

3.18 Section 49 of the Consumer Credit Act 1974 (CCA) prohibits the canvassing and soliciting of cash loans off trade premises where this is not done in response to a signed written request made on a previous occasion. This applies to existing customers as well as new customers.

3.19 Some firms currently obtain consumers' written permission when they first enter into the credit agreement. Firms then treat this as an ongoing 'permission to call' or 'umbrella request' for the rest of the agreement, sometimes lasting even after the consumer has paid off their loan. They use this as proof that the consumer has made a written request to discuss further loans at any point in the future, and believe that they can then suggest further lending to consumers within the home at any time while the permission is valid.

3.20 We believe this practice breaches s.49 CCA. We do not consider that a visit based on a non-specific 'permission to call' is a visit made in response to a request within the meaning of s.49 CCA. In our view this undermines the consumer protection objective of the law, of ensuring that consumers are in control over whether they want to discuss new or additional borrowing. In addition, some consumers have reported that firms' representatives are proactively offering further borrowing without this being in response to a specific request. We therefore consider that guidance is needed to clarify the law in this area. Although we note that only a court can give a definitive interpretation of the statutory provisions.

3.21 We are consulting on new guidance which sets out our interpretation of s.49 CCA and how it applies to existing customers. Firms must be aware of this prohibition when they consider discussing or entering into new credit agreements with consumers during visits to collect repayments under an existing loan, or at other times. The proposed guidance is set out in Appendix 1.

Questions for consultation

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

Refinancing

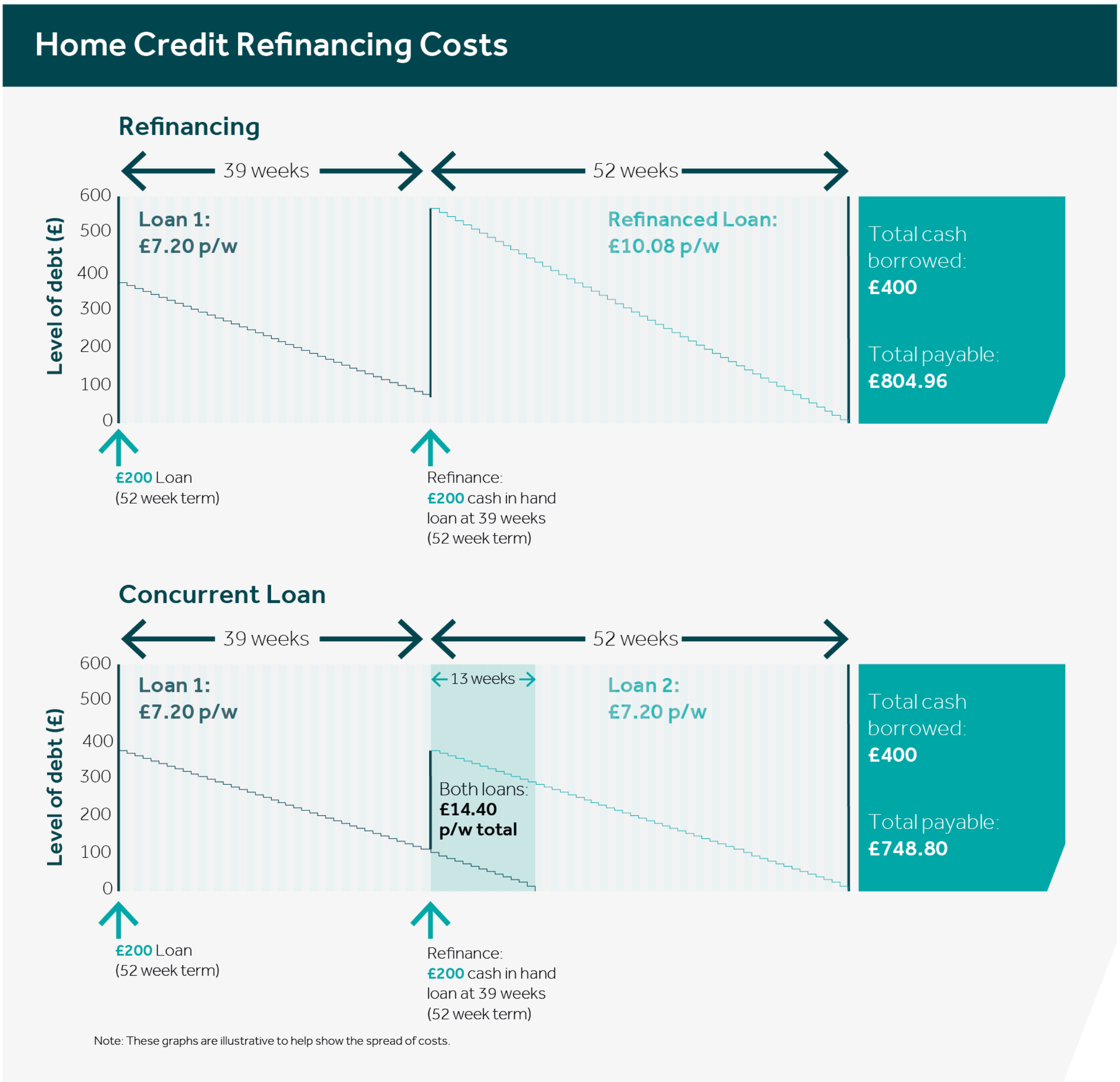
3.22 We also have concerns over the way in which consumers access further borrowing. Many consumers refinance existing loans enabling them to keep weekly repayments the same or as low as possible. The new loan is used to repay the outstanding amount of the existing loan. If the consumer wants their weekly repayments to remain the same they will generally receive a lower cash-in-hand amount as a result. Approximately 30-40% of all home-collected credit loans are refinanced with additional borrowing.[22]

3.23 The total costs of refinancing are greater than taking out an additional loan. This is partly due to the way that early settlement rebates are calculated. Early settlement rebates compensate consumers for overpaying interest during the course of the loan, where interest payments are prioritised over reducing capital in a typical amortisation schedule. Consumers will also borrow more to pay off the outstanding balance on the loan, which generates additional interest charges. Table 3.1 sets out a comparison of the costs of refinancing a loan with the cost of taking an additional, overlapping, loan.

Table 3.1: Illustration of comparative costs of refinancing vs. concurrent loan

Customer seeking additional £200 cash in hand at week 39 of a 52 week £200 loan (total payable of £374.40, weekly repayment £7.20)		
39 weeks	Refinance	Concurrent
First loan amount paid	£280.80	£280.80
First loan amount due	£93.60	£93.60
Rebate given to consumer (statutory only)	£11.45	N/A
Settlement figure (to be "rolled up" into refinanced loan)	£82.15	N/A
Second loan principal	£280 (52 weeks)	£200 (52 weeks)
Second cash in hand	£197.85 (remainder pays off Loan 1)	£200
Second loan interest	£244.16	£174.40
Second loan total payable	£524.16	£374.40
Weekly Repayments	£10.08	£14.40 reverting to £7.20 after 13 weeks
Principal repaid (both loans)	£401.93	£400
Interest due (both loans)	£403.03	£348.80
Total payable (both loans)	£804.96	£748.80

22 This is based on data we collected from five of the largest firms in the sector on their rates of refinancing across 2015-17.



3.24 Most firms we spoke to acknowledged there are risks to consumers of potential additional costs and most have policies in place to protect consumers from potential financial harm caused by refinancing and to reduce the risk of cycles of unsustainable debt. These include:

- Specifying that consumers can only refinance when a certain proportion of the previous loan has been repaid. For the firms we surveyed, this proportion ranged from 40% to 66%. Our analysis found that very few loans (less than 4%) were refinanced before 50% of the initial loan had been paid down.
- Minimum limits for the amount of a refinanced loan that the consumer must receive 'cash in hand', with the remainder rolled into the new loan. Firms state that this helps to ensure refinancing is driven by a genuine borrowing need.
- Minimum collection rates for recent repayments to ensure that consumers at risk of financial difficulties are not able to borrow more.

- Customers receive an early settlement rebate as required by the early settlement regulations. The rebate is typically the interest initially charged for the period between the early settlement date and the contractual end-date, minus thirteen days interest.[23] Some firms give more than the statutory minimum rebate, but many still keep thirteen days interest payments in accordance with the regulations.

- Other restrictions included thresholds for lending only up to a proportion of remaining disposable income per week.

3.25 Some firms have measures in place to discourage customers from refinancing altogether because of the potential for consumers to pay interest on interest and pay down the principal more slowly.

3.26 There are currently several rules in place relevant to repeat borrowing:

- A requirement for firms to assess creditworthiness, including affordability, every time a customer refinances a loan or takes additional borrowing (CONC 5.2 and 6.2). This distinguishes fixed sum credit from running account credit, such as credit cards, where users can get additional credit within their credit limit without a further affordability assessment.

- A rule prohibiting firms from encouraging customers to refinance where this would make the customer's commitments unsustainable (CONC 6.7.18).

- A rule preventing refinancing unless the firm does so at the customer's request or with their consent (CONC 6.7.19).

- A rule preventing firms from refinancing unless they reasonably believe it is not against the customer's best interests to do so (CONC 6.7.19).

3.27 Despite these protections, we are concerned that there remains unacceptable risk to consumers from the incentives firms have to influence consumers to borrow again and to do so in a way that is more costly for them.

3.28 In many firms, refinancing loans generates commission for firm representatives, including on settlement figures. We are concerned that this means consumers are channelled towards refinancing because it generates more income for firms, and potentially higher commission for firm representatives. Our consumer research also revealed that consumers generally had a poor understanding of what point they are at in the loan term and tend to rely on firm representatives for this information.

3.29 Our recent consultation on new rules to help consumer credit firms identify and appreciate the risks their staff incentives pose to consumer outcomes and to help firms understand what is expected of them should mitigate some of the potential for harm here, and we will monitor how the rules are being implemented by firms and the impact this is having.[24]

3.30 We consider that there are additional measures firms should take to help consumers understand the costs of different forms of repeat borrowing. We know that many consumers focus on maintaining weekly repayments to budget and manage their

23 This was amended by the Competition Commission's investigation into home-collected credit to ensure consumers are given a larger rebate than the minimum required by CCA regulations.

24 www.fca.org.uk/publication/consultation/cp17-20.pdf

weekly spending when considering further loans. This is a common theme among users of high-cost credit who are often living on limited or irregular incomes. This would suggest they prefer refinancing, rather than taking another loan which would increase their weekly repayments.

3.31 But our consumer research also shows some consumers do not know they could get additional borrowing from the same firm, or that it may be cheaper for them in the long term to take out a concurrent loan rather than refinancing. They are also not always aware of the benefits of waiting until the end of their current loan term before borrowing again. Although some firms have suggested that consumers would prefer the simplicity of only having one outstanding loan to manage, data from firms shows that on average 46% of their consumers are holding more than one loan at a time from the same firm.

New information requirements for refinancing and further borrowing

3.32 We are proposing a new requirement for firms when they discuss further borrowing with consumers. This will require them to set out and explain the loan options that are available and the comparative costs of refinancing as opposed to taking out an additional loan.

3.33 This will allow consumers to be better informed on their alternative borrowing options and their costs. With this information, some consumers may feel they have the flexibility in their budget to pay more in weekly repayments for a shorter time to reduce the total costs of borrowing.

3.34 Under our proposal, firms will give a verbal explanation of the borrowing options and a written notice setting out the difference in costs in terms of both weekly repayments and the total amount payable. We consider that this is the best approach to ensure consumers understand the options available. We are not being prescriptive on how firms must present or communicate this written disclosure, but they must include the required content in a way that is clear and not misleading. Where the firm representative shows the consumer information on an app or on an electronic device, the representative should also provide information in a durable medium for the consumer to keep so that they can consider the information following the visit and decide whether they wish to proceed.

3.35 We know that some consumers may not be eligible for certain loan options. For example, a firm may decide that a consumer probably won't be able to afford an additional loan that would increase their weekly repayments and would therefore fail a creditworthiness assessment. Conversely, some consumers may not be eligible to refinance. This might be, for example, if they are at an early stage of repaying an initial loan or if the cash in hand amount they want to borrow does not satisfy the firm's polices on refinancing. In such circumstances we would not expect firms to have to give information about options which are not available to the consumer.

3.36 This remedy addresses the lack of information for consumers and potential misaligned incentives for firms to encourage customers to refinance loans when they want to borrow more. Firms are currently likely to know that refinancing is more expensive in total costs than taking out the equivalent borrowing through an additional separate loan. We propose that the rules come into force three months after publication.

3.37 We have considered whether more interventionist measures may be appropriate. These could include, for example, putting a limit on refinancing or specifying when in the loan cycle firms may refinance (eg not before 75% of the initial loan has been paid down). However, this would have the effect of limiting access to credit which may be needed for emergencies. At this stage we therefore do not propose to pursue this option.

3.38 We have also considered whether there is a case to undertake the work that would be necessary to assess whether to introduce a price cap, and have decided that, on balance, there is currently not. While the costs for some consumers can accumulate, this is the result of how some firms refinance consumers' loans, rather than the pricing of individual loans. Our proposals aim to address this source of harm directly and we would expect to see reductions in the cumulative cost paid by consumers. We are therefore not currently planning to develop proposals for a price-cap for home-collected credit, but will revisit this issue when we assess the effectiveness of the changes we are now proposing.

Questions for consultation

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

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

Next steps

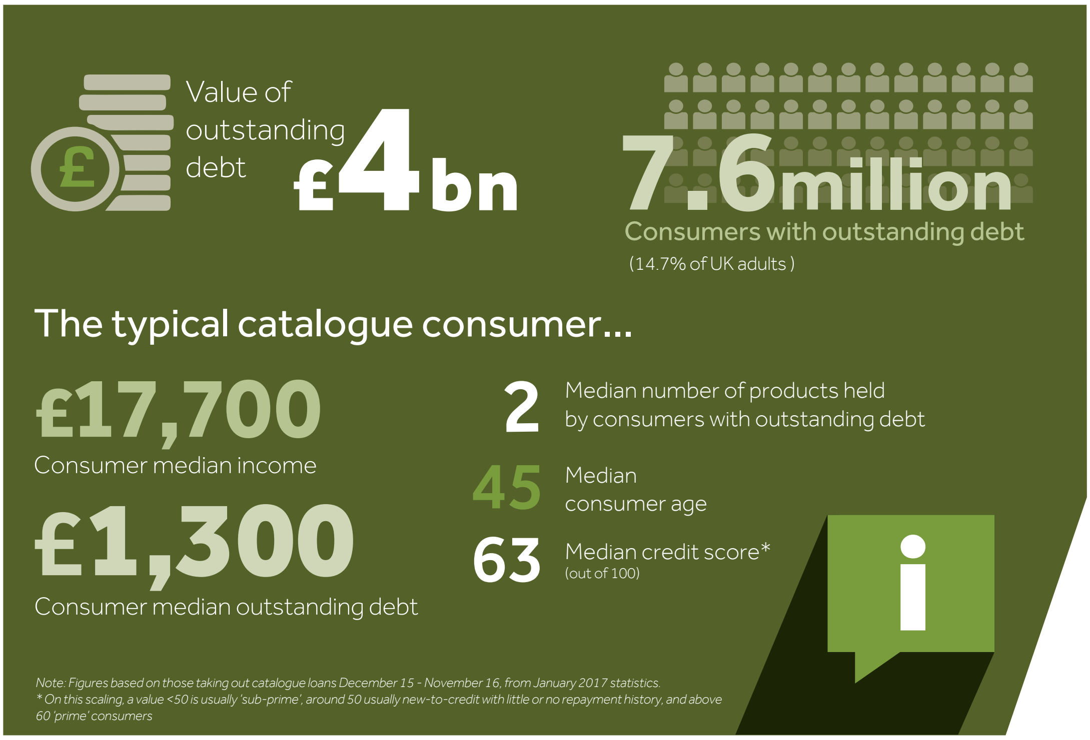
3.39 Please respond to the consultation questions (Q8-10) on our proposals for home-collected credit by 31 August, submitting your responses to cp18-12@fca.org.uk. Subject to the responses to consultation that we receive, we aim to finalise these rules and guidance in Autumn, with the rules coming into force early in 2019.

4 Catalogue Credit and Store Cards

Summary

4.1 Catalogue credit (also known as mail order or home shopping) is a form of running account credit to buy goods and services from specific retailers. Retailers provide online and hard-copy catalogues from which consumers buy goods.

Consumers who use Catalogue credit[25]



4.2 In the first phase of the review we identified catalogue credit as a product for further work. This was due to the high level of borrowers' arrears, the fees and charges that are triggered by arrears and the related risk of financial distress. We also found firms charging high levels of interest outside interest-free periods and have looked in more depth at the impact on borrowers and the transparency around interest-free periods.

4.3 Since then, we have considered whether the similarities between catalogue credit and store cards create similar risks for consumers of each. There are some differences in the consumer demographic for store cards compared with catalogue credit. Both have similar median income, but store card customers have slightly lower median outstanding debt (at £1,100) and a lower median debt to income ratio (8% compared with 28%).[26] Store card customers have a lower median age of 36, compared with 45 for

25 Feedback Statement: High-cost credit including review of the HCSTC price-cap, FCA, July 2017 https://www.fca.org.uk/publication/feedback/fs17-02.pdf

26 The debt to income ratio is the total outstanding personal debt to estimated annual, net individual income (DTI) ratio. It does not include mortgage cost.

catalogue credit, and a lower proportion of customers live in rented accommodation. There are also some differences in the patterns of use, for example there is on average a smaller proportion of store card consumers in debt after 24 months.

4.4 There are also differences in the business model. The store card model is to provide rewards for customer loyalty as well as being a payment mechanism, whereas the catalogue credit model is retail driven by credit sales. Store card credit tends to be provided by a third party, whilst catalogue credit firms have both retail and credit operations within the same group.

4.5 Despite these differences, we see similar risks to consumers from using a running account linked to specific retail purchases and have included store cards in our proposals. Within both catalogue and store card sectors different practices by firms may lessen these risks, but there is no clear cut dividing line between the two sectors in terms of risks to consumers.

4.6 We collected and analysed a range of data to explore these issues:

- a firm questionnaire sent to the majority of catalogue credit and store card firms in the market
- consumer research which looked at consumers' experiences and perceptions of catalogue credit and store cards
- evidence from our ongoing supervision work
- meetings with industry bodies and their catalogue credit and store card members
- credit reference agency data analysis on catalogue credit and store card customers and their debt portfolios

4.7 In this chapter, we set out our findings on harm for consumers of catalogue credit and store cards, and how our proposals will address them.

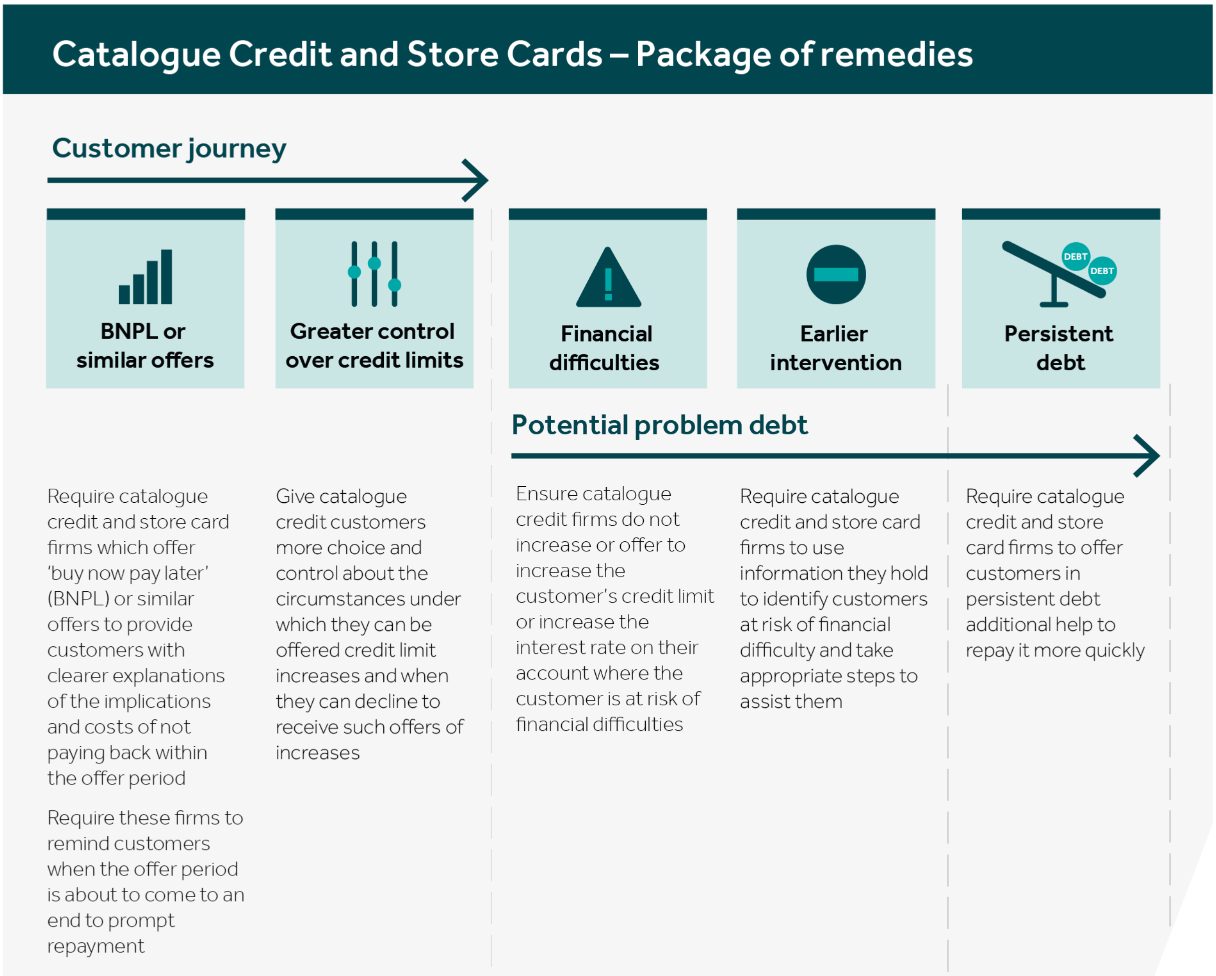
Findings

4.8 We have identified the following issues as key areas of concern:

- **Credit offers** – consumers don't know, or are not factoring into their decision-making, that interest may be charged from the date of purchase (backdated) and potentially payable on the entire purchase amount (even if part payments have been made) if they fail to repay the full purchase price within the interest free time period for repayment offers such as BNPL.
- **Consumer choice and control over credit limit increases** – catalogue credit customers are not given sufficient choice and control over credit limit increases.
- **Treatment of consumers at risk of financial difficulty** – there is evidence that catalogue credit firms give credit limit increases to consumers in financial difficulty.

- **Potential problem debt** – flexible repayment terms mask financial difficulties and debt held over a long period incurs high costs.

4.9 Our proposed package to address these issues is summarised below.



Credit offers

4.10 A small number of catalogue credit and store cards firms offer BNPL deals or similar offers. These offer the consumer a promotional period, typically up to 12 months, during which no interest is charged. However, if the consumer fails to repay the entire amount within this period, then interest will typically be charged on the whole balance or the unpaid part of the balance from the date of purchase.

4.11 Our consumer research highlighted that BNPL deals are often attractive for consumers, as there is no obligation to make repayments during the offer period and interest is waived if you repay in full in the period. However, there were examples of both catalogue credit and store card customers over-estimating their ability to steadily pay off these debts and incurring interest as a result. Many did not regard store cards or catalogue credit as feeling like 'real money' and as such did not really perceive it as a form of borrowing. Some consumers said this was because they didn't understand how interest charges worked and the impact this had on what they were charged after any interest free period. In some cases, this led to 'unexpected' spiralling debt on consumers' accounts and a knock-on effect on their credit score.

4.12 Typically, around half of consumers do not repay within the offer period, incurring interest charged on the whole balance or the unpaid part of the balance from the date of purchase as a result.

4.13 We have fundamental concerns over the practice of charging on the whole balance from the date of purchase in the event that a consumer fails to repay the entire amount for BNPL and similar offers. We are concerned that the nature of BNPL means that whilst some consumers benefit, others incur high costs. Ensuring consumers are clear about the consequences of taking up the offer and giving them opportunities and incentives to repay within the offer period are essential to protect consumers.

4.14 We have looked at the information firms give consumers on BNPL offers. We think that firms could be clearer about the consequences of not repaying within the offer period, in particular that a lump sum of interest will be added to their account. We also think that firms could give more prominent reminders to consumers to repay within the offer period.

4.15 Existing rules require firms to give an adequate explanation of specific matters, including features of the agreement which may have potential adverse consequences in a way that consumers would be unlikely to foresee.[27] We propose to extend the existing rule to make it clear that this includes how interest will be charged if the consumer does not repay within the BNPL offer period.

4.16 We propose a further new rule requiring firms[28] to provide clear, prominent and timely notice to the customer before the end of a BNPL or similar offer that depends on the consumer meeting certain conditions. This notice must be provided in an appropriate medium that takes into account any preferences expressed by the customer about the medium of communication between the firm and customer. It should also be in plain language and sufficiently prominent so that it is likely to be seen and understood by the customer, for example upfront in a monthly statement or through text alerts. We do not propose specifying a time period. Firms should judge the most appropriate time to notify customers to achieve the objective of prompting repayment.

4.17 Implementing the proposals will require firms to make changes to the information they provide to consumers online and in hard copy. We propose that the rules come into force three months after publication.

4.18 We note that BNPL offers are used on other retail credit products. This is an issue where we are planning further work, taking a broader look across those products and the outcomes for consumers. As part of this, we will consider the information that is provided to consumers on BNPL and similar offers during the agreement and whether additional measures are warranted.

Questions for consultation

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

27 CONC 4.2.5R(2)(c)

28 This rule will not apply to firms subject to Part 6 to the Payment Services Regulations 2017. There are certain exclusions from the Payment Services Regulations which are likely to apply to retail revolving credit such as paragraphs 2(k)(i) to (iii) of Schedule 1 to the Payment Services Regulations 2017 (activities involving limited network payment instruments which do not constitute payment services).

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

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

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

Q15: **Do you have any comments on our proposals for a three month implementation period?**

Consumer choice and control over credit limit increases

4.19 Many catalogue credit and store card firms provide or offer credit limit increases.

4.20 Typically, starting credit limits are low. Our research found starting credit limits were on average less than £500 for catalogue credit users. For store card users they were between £100 and £1,000, with only a few being more than £1,000.

4.21 There are approximately 600,000 new catalogue credit accounts opened each quarter and most credit limit changes are in the first year of opening. In Q1 2014 almost 75% of catalogue accounts had a least one credit limit increase and many had more than one. Using this data, we estimate that there are at least 2.8 million credit limit increases a year for new consumers over the first two years. Approximately 50% of these credit limit increases were of £200. The proportion of accounts with credit limit increases for store cards is less (with 72% having no credit limit increases over the same period).

4.22 Our consumer research indicates that consumers can see credit limit increases as a temptation to spend more than planned or affordable and find this hard to resist. More compulsive consumers said that credit limit increases led to increased spending.

4.23 We have concerns that credit limits may be increased for catalogue credit customers without consulting them or telling them in advance. If consumers cannot control when credit limit increases are introduced, then some may spend more than they would otherwise plan to. Consumers in our research said they would prefer being told about a credit limit increase in advance with the opportunity to opt out to avoid the temptation of having extra credit.

4.24 Existing rules that apply to credit cards and store cards limit the circumstances when a firm can provide or offer a credit limit to customers. These rules are:

- firms must not increase or offer to increase the customer's credit limit where they have been advised that the customer does not want to have any credit limit increases
- firms must permit a customer to reduce or decline offers to increase the credit limit
- firms must tell the customer of a proposed increase in the credit limit under the agreement at least 30 days before the increase comes into effect unless the:

- customer has expressly requested the increase
- firm has proposed the increase, but the customer agrees to it at the time and wants it to come into effect in less than 30 days

4.25 Most catalogue credit firms in our sample said that they already voluntarily follow this approach. However, we think it is necessary that consumers have the same framework to control whether and how credit limit increases are applied over the different types of running account credit they may have. We are therefore proposing to extend these rules to catalogue credit firms.

4.26 We expect that implementing these rules will require changes to the information firms currently give customers, as well as system changes to ensure that customers are given greater control. We propose that the rules come into force three months after publication.

4.27 The industry bodies representing catalogue credit and store card firms, the Finance and Leasing Association (FLA) and the British Retail Consortium (BRC), have also said they are willing to discuss a voluntary industry agreement for their members similar to that agreed for credit cards.[29] This would give consumers further control over how they are offered credit limit increases. For example, under the credit card voluntary agreement existing customers have the ability to tell firms that they want to only accept offers of credit limit increase on an opt-in basis, rather than have firms automatically increasing it if they do not reject the offer (opt-out). New customers are also given the choice of how increases are offered, with existing customers given a more straightforward means to decline an increase and choice of how these are offered. We will continue to discuss this with the FLA and BRC.

Questions for consultation

Q16: **Do you have any comments on our proposals to extend the existing rules for credit cards and store cards regarding credit limit increases to catalogue credit?**

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

Treatment of consumers at risk of financial difficulty

4.28 We have evidence that some catalogue credit customers in financial difficulties have been offered credit limit increases.

4.29 We do not think it is appropriate that consumers at risk of financial difficulties have more credit made available to them which may result in unmanageable debt. We also want to ensure that firms are not increasing the rate of interest on consumer accounts where they are at risk of financial difficulties. To do so is likely to compound their problems.

4.30 Firms told us that they did not give credit limit increases to consumers at risk of financial difficulties. Yet we have had some complaints made to us from consumers

29 https://www.fca.org.uk/publication/consultation/cp17-43.pdf paragraphs 4.7-4.8

that they or their family members had received credit limit increases despite clear signs that they were in financial difficulty. We also have evidence from analysing the CRA data for catalogue credit that there were approximately 7,800 credit limit increases in the 2016 cohort where the consumer was two or more payments in arrears.

4.31 We, therefore, consider there is a clear need for a new rule to prevent this from happening.

4.32 Existing rules apply to credit card and store card firms which ban them from increasing credit limits[30] or interest rates[31] for consumers who are at risk of financial difficulties. This is defined as where a consumer is two or more payments in arrears, or has agreed a repayment plan, or is in serious discussion with a firm which carries out debt counselling with a view to entering into a debt arrangement plan and the firm has been notified of this fact. We propose extending these rules to catalogue credit firms. We consider that this extension is necessary to reflect the high delinquency rate for catalogue credit. CRA data shows that the proportion of agreements where consumers miss two (or more) payments rises above 15% after 12 months from credit origination.

4.33 Implementing the proposals will require firms to ensure that they have adequate processes to identify those at risk of financial difficulty. However, we consider that firms should already have these systems in place because of the requirement to monitor a customer's repayments for signs of financial difficulty. We consider that the risk of harm from credit limit increases and interest rate increases is high. Therefore, we propose that firms will have to take steps immediately to be compliant with the rules after they come into force.

Questions for consultation

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

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

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

Earlier intervention

4.34 Catalogue credit and store card firms are currently required to monitor a customer's repayment record for signs of actual or possible financial difficulties. However, the flexible repayments allowed on both of these products may mask possible financial difficulties. Because consumers' minimum repayments can be low, once they start to miss repayments they may already have been in financial difficulty for some time.

30 CONC 6.7.7(2)R
31 CONC 6.7.10R

4.35 This was also a key risk identified in our credit card market study. This led us to publish new rules to require earlier intervention by credit card firms. These require that firms should monitor the information available to them to identify and take appropriate action to support consumers at risk of financial difficulties.

4.36 Catalogue credit and store card firms already use some earlier intervention strategies to support consumers who show signs of financial difficulty and monitor a range of information to identify consumers at risk. However, we think there is more that firms can do to intervene at an earlier stage so that fewer consumers end up in arrears or default. The high arrears rates particularly in the catalogue sector[32] suggest that this is an area where there is substantial scope for firms to do better.

4.37 We therefore propose to extend the rules on earlier intervention to ensure a consistent standard across the catalogue credit and store card markets.

4.38 The proposed new rules build on the existing rule that requires firms to monitor a consumer's repayment record for signs of actual or potential financial difficulties.

4.39 They are made up of three elements:

- catalogue credit and store card firms will be required to monitor a consumer's repayment record and any other relevant information they hold to identify signs of actual or possible financial difficulties
- firms must take appropriate action where there are such signs
- firms must establish, implement and maintain an adequate policy for identifying and dealing with consumers showing signs of actual or possible financial difficulties, even though they may not have missed a payment

4.40 We are aware from our firm survey that firms monitor a variety of historic and ongoing drawdown behaviour including payments (satisfied, missed, late or insufficient) and credit limit utilisation.

4.41 As with credit cards we do not propose to specify in rules or guidance particular aspects of account activity that firms should monitor, as they will be best placed to identify appropriate indicators.

4.42 We propose that firms have to comply with these rules 6 months after they come into force. We think this is the right balance between firms putting in place processes to deal with the new requirements and acting quickly to protect consumers.

Questions for consultation

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

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

32 As noted in our technical annex to our feedback statement, around 30% of catalogue credit agreements went into arrears during 2012 to 2015 and around 20% of store card agreements went into arrears during the same period.

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

Persistent debt

4.43 One of the key features of both catalogue credit and store cards is that consumers can typically decide how much to repay as long as they meet the minimum repayment. This flexibility allows consumers to repay in full at the end of each month or to spread payments over a longer period.

4.44 But this flexibility also means it is possible for consumers to carry a large balance for a long time without significantly reducing their debt.

4.45 This was also one of the key risks that we identified in the credit card market study. We recently published new rules for credit cards to address the problem of consumers who were in 'persistent debt'. We define persistent debt for credit cards as the circumstances where, over a period of 18 months, a consumer pays more in interest and charges than they have repaid of the principal.

4.46 We had concerns that consumers may also be falling within the definition of persistent debt on catalogue credit and store card products.

4.47 There are some differences in the product features of catalogue credit and store cards and the way consumers use them that could mean this is less likely. These are:

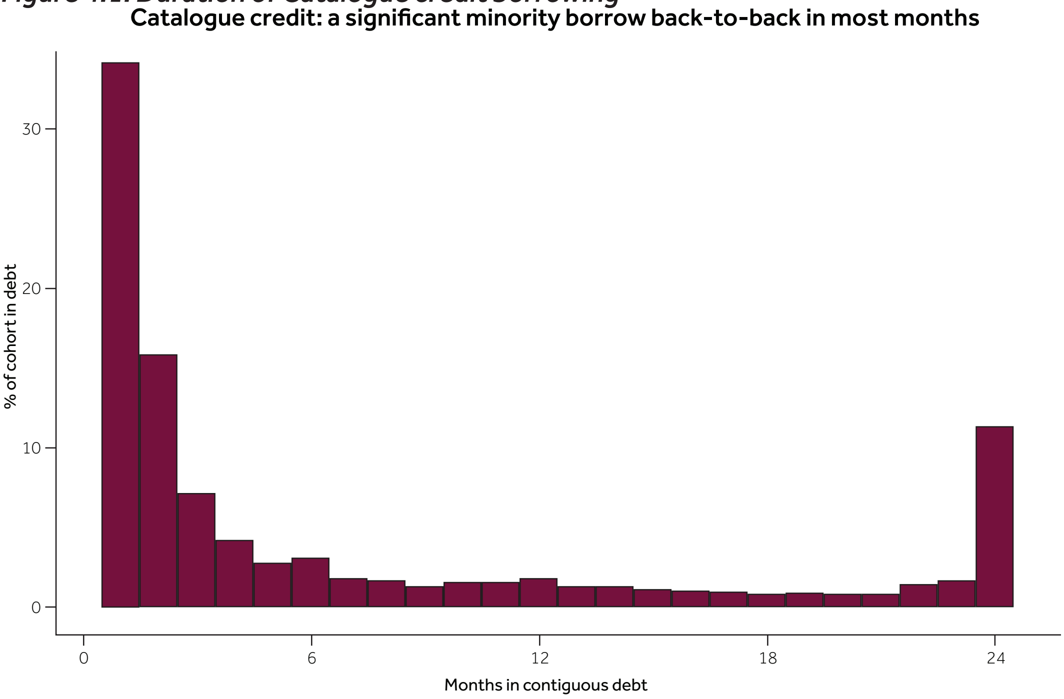
- The product is linked to specific purchases of a limited range of goods, unlike credit cards which are a widely accepted payment mechanism. This makes it more likely that a consumer would buy goods and then largely or completely repay before making the next purchase.
- Minimum repayments tend to be higher than in the credit card market for both catalogue credit and store cards. This makes it more likely that consumers will pay down within a reasonable period.
- Average balances are lower (£856.50 for catalogue credit and £834.20 for store cards), again making it more likely that consumers will be able to pay down more quickly.

4.48 On assessing the evidence, we found that, despite these differences, some consumers using catalogue credit and store cards do fall into persistent debt.

4.49 We first analysed the CRA data to assess the overall repayment profiles for catalogue credit and store card consumers. We tracked a set of consumers who opened an account in Q1 2014 over a 24 month period and looked at their spells of time in debt (ie a continuous period of indebtedness month to month).

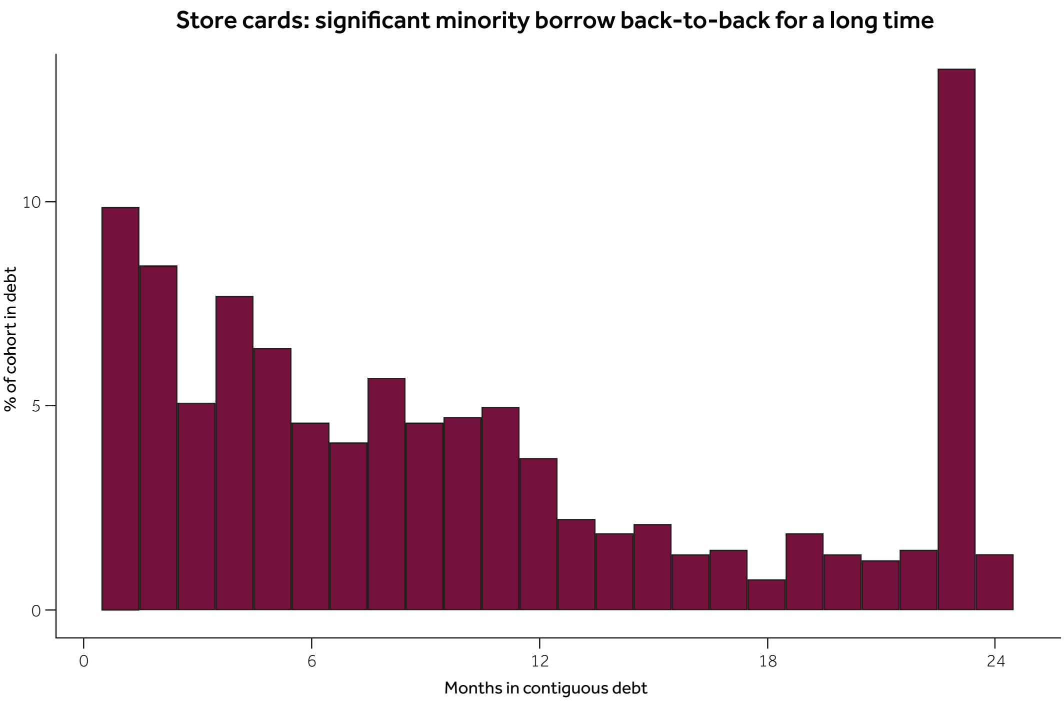
4.50 For those catalogue credit consumers who went into debt at some point, the median number of months in contiguous debt was 3, and the majority (57%) were in a debt spell for 3 months or less (see Figure 4.1). However, 11% were indebted every month over a 24 month period.

Figure 4.1: Duration of Catalogue credit borrowing



4.51 There is a slightly different picture for store cards (Figure 4.2). Of those consumers in the cohort who went into debt at some point, the median consumer was in continuous debt for a duration of 9 months in the 24 month period we examined. 23% were in continuous debt for an average of 3 months or less. However, 21% were in continuous debt for 18 months or more in a 24 month period.

Figure 4.2: Duration of store card borrowing



4.52 These indebtedness patterns suggest that a proportion of consumers do borrow and repay in a way which can lead to prolonged indebtedness. This was borne out by the data from firms on levels of persistent debt.

4.53 We asked a sample of firms to provide us with the numbers of their customers who would fall within the definition of persistent debt on 1 November 2017. These firms covered over 70% of the catalogue credit and over 90% of the store card markets. We scaled these results to give an overall estimate for each market.[33]

Table 4.1 Customers in persistent debt

Market	Number of customers in persistent debt at the 18 month mark (millions)	Number of customers in persistent debt at the 36 month mark (millions)	Average balance of customers in persistent debt
Catalogue credit	0.34 (6%)	0.18 (3%)	£848.08
Store card	0.29 (7%)	0.18 (4%)	£841.31
Total	0.62 (6%)	0.36 (3%)	£844.96

4.54 Comparing these figures with credit cards, we found that more than 3.3 million credit card customers with a total of 4 million accounts would fall into the definition of persistent debt at 18 months. Of these, 1.8 million customers would be in persistent debt 18 months later. On average, a credit card account in persistent debt had a closing balance of £3,464.

4.55 Catalogue credit and store card firms vary considerably in the proportions of their customers falling within the definition of persistent debt. This ranged from less than 0.5% to above 3.5%. We expect this to be largely influenced by different firm policies on minimum repayment. Customers with store cards are more likely to stay in persistent debt for 36 months because on average there is a lower minimum repayment across the sector.

4.56 The consumer research showed that for some consumers, there is a tendency to think that if they are making minimum repayments, they are doing enough. Whilst they were generally aware that faster repayment would be cheaper there was limited incentive to do so.

4.57 We think that consumers in persistent debt, whether they are holding the debt on credit cards, catalogue credit or store cards, need to be prompted and helped to repay their debts more quickly. Firms need to do more to help consumers recognise the benefits of lower costs if they repay their debts more quickly and to discourage long term use of flexible repayment terms which are designed to manage temporary changes to consumers' budgets.

4.58 We recognise that the average balance of a catalogue and store card customer is relatively low and significantly lower than a credit card customer in persistent debt. However, this does not impact on the fact that catalogue and store card credit are not appropriate to use as long term borrowing products. Our proposals should also make it easier for firms to help consumers find an appropriate way of managing their way out of persistent debt. Where firms have small numbers of consumers in persistent debt, we expect that it will be relatively low cost for them to support consumers to avoid or resolve persistent debt.

33 The methodology is set out in our CBA in Annex 2

Proposed rules – persistent debt

4.59 We propose to extend the rules on persistent debt that currently apply to credit cards to catalogue credit and store cards.

Definition

4.60 We propose to define persistent debt as where over a period of 18 months a consumer pays more in interest, fees and charges than they have repaid of the principal. We consider that this definition is appropriate to capture the problem of incurring high cost from holding a short term debt over a long term.

4.61 The period of 18 months has been chosen to enable seasonal variations in spending and income that extend beyond a calendar year to be captured and to enable persistent patterns of repayment to emerge. For catalogue credit and store cards, it takes into account of the fact that BNPL offers may run for 6 or 12 months and a consumer's repayment pattern may not be established for the first 12 months after opening their account.

4.62 We propose that consumers whose balance has fallen below £200 at any point during the 18 months are excluded. We consider this minimum balance is appropriate for catalogue credit and store cards. Whilst average balances are significantly lower than for credit cards, we consider that the benefits of intervention are likely to be offset by the administrative costs. Catalogue credit and store card firms also typically stipulate that a minimum repayment cannot be less than £5. Once the minimum is hit, typically at a balance of £200, the ratio of repayment and principal reduces quickly.

Intervention at 18 months

4.63 We propose that at 18 months, firms would need to prompt consumers in persistent debt to change their repayment behaviour if they can afford to. Consumers would be made aware of the potential implications of continuing to make low repayments. The firm would also give the consumer the contact details of sources of debt advice. Our consumer research indicated that consumers make minimum repayments in the belief that they have done what is necessary, without considering the cost implications. The intervention would encourage consumers to consider repaying more quickly and, if they cannot afford to do so, to encourage consumers to seek debt advice and discuss their circumstances with the firm.

Action at 27-28 months

4.64 At 27-28 months, firms would send a further reminder if payments indicate the consumer is still likely to be in persistent debt at the 36 month point.

Intervention at 36 months

4.65 We consider that further intervention is appropriate at 36 months if a consumer remains in persistent debt. Firms would need to help the consumer by proposing ways of repaying more quickly over a reasonable period. Where the consumer is unable to repay more quickly, the firm must show forbearance if they have not already done so (for example, by reducing, waiving or cancelling any interest or charges). We would expect firms to suspend the accounts of consumers that have been shown forbearance and of those who do not respond.

4.66 Whilst there is presently a substantial reduction in the numbers in persistent debt between 18 and 36 months, we believe firms need to step in to support consumers who have paid a substantial amount of interest and charges over the three year period, but have still repaid very little of the principal.

Reasonable repayment period

4.67 We are intending to adapt the guidance used for credit cards in respect of the reasonable repayment period of three to four years for catalogue credit. Because balances are smaller, this may be too long. We propose that the guidance sets out that a shorter repayment period is likely to be appropriate for catalogue credit. We propose to keep the guidance that sets out that we would expect the repayment period to extend beyond four years only in exceptional circumstances.

Implementation

4.68 We want firms to take action quickly to help consumers who are already in persistent debt. At the same time, we recognise that firms will have to implement processes for identifying those in persistent debt. We propose that firms will have to comply with the rules 6 months after they come into force. This means that on this date, firms will have to assess which consumers have been in persistent debt for the previous 18 months. The period would include the 12 months before the rules came into force. The proposed implementation timetable also means the first 36 month interventions will occur 24 months after the rules come into force.

Questions for consultation

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

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

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

Definition

4.69 We want to ensure the rules we are proposing apply to catalogue credit and store cards including any goods and services that they may provide under their agreements with consumers. From our research and our discussions with stakeholders we recognise that these markets are evolving. Consequently we propose a wider definition of retail revolving credit to reflect this particular form of running account credit where its use is limited. We propose that this definition would consist of:

- a running account credit agreement
- restricted to paying for goods, or for goods and services – not services only [34]
- from a particular supplier or group of suppliers

34 We have not considered retail running account credit for the purchase of services only as part of our review and have consequently excluded this from the definition.

4.70 It would include where the agreement is an agreement for a store card but exclude a credit card.

Questions for consultation

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

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

Next steps

4.71 Please respond to the consultation questions (Q11-28) on our proposals for catalogue credit and store cards by 31 August, submitting your responses to cp18-12@fca.org.uk. Subject to the responses to consultation that we receive, we aim to finalise these rules and guidance in Autumn, with the rules coming into force early in 2019.

5 Alternatives to high-cost credit

Summary

5.1 An essential part of our overall package is the work we are doing to foster the growth of alternatives to high-cost credit. Greater availability and awareness of alternatives would reduce the number of people turning to high-cost credit services. It would also provide options for consumers who may no longer be able to access high-cost credit services after any possible interventions we make. Greater availability of alternatives would therefore help consumers get a better outcome.

5.2 In our January 2018 update, we set out the barriers to providing relatively lower cost, mid-price alternatives and the actions that we could take to address these. This chapter provides an update on the actions we have taken and are proposing to take.

5.3 We cannot solve these issues alone. We are working with a number of public agencies to develop more effective approaches to the problems we have identified. We have engaged widely in discussions with stakeholders across Government and beyond to encourage and support initiatives that could increase the availability and diversity of alternatives to high-cost credit, and will continue to do so.

5.4 One area where we can act directly is in encouraging referrals to alternative sources of credit by making sure there is clear guidance available on the regulatory implications of doing so. We are consulting in this CP on guidance to give registered social landlords (RSLs) confidence over the steps they need to take when they refer their tenants to alternatives such as credit unions and CDFIs. Our objective is that at critical points, such as when tenants move into a new property, RSLs are in a position to inform the tenants about their options for furnishing it.

The social value of alternatives to high-cost credit

5.5 We recognise the value of high-cost credit for consumers who lack other options, where firms have made an appropriate assessment of their creditworthiness. However, we are also exploring why relatively lower cost, mid-price, lower risk credit options are not more widely available. We have been looking at barriers to providing alternatives and considering what might be done to address these.

Barriers to providing alternatives

5.6 Table 5.1 summarises the barriers we have identified to the development of alternatives to high-cost credit that we set out in our January update.

Table 5.1: Barriers to alternatives to high-cost credit

Barrier	Summary
Access to sustainable capital	The costs and risks of providing small loans create particular funding challenges. The sector needs to be self-sustaining in order to offer the prospect of expansion and long term service to consumers rather than relying on grants, although we have seen evidence of 'pump-priming[35]' being effective.
Alternative credit as a financial inclusion tool	Credit is not universally accepted as a useful service for the financially vulnerable. Investors, donors, local authorities and others who might otherwise help in expanding the reach of alternative credit schemes can be wary of extending credit to high-risk borrowers and the risks of increasing indebtedness.
Varying appetite and capacity amongst credit unions to lend to higher risk consumers	Credit unions are diverse, with different risk appetites and capacity to expand their lending into higher risk groups. Some larger credit unions successfully partner with CDFIs, alongside other local-level not-for-profit partners, but there is no easy route to replicating this.
Uncertainty about regulatory requirements	Stakeholders told us that use of alternative credit works best for the financially vulnerable as part of a package of support services. However, uncertainty about the regulatory boundary and requirements can deter support services from making referrals.
Connecting at key moments	Part of the demand for high-cost credit is driven by consumers moving in at short notice to unfurnished social housing tenancies. While there are some successful schemes set up by local authorities and other registered social landlords (RSLs) to provide essential goods to tenants, there is no formal or widespread mechanism for sharing best practice and expertise. A fear of the burden of regulatory requirements may act as a barrier to RSLs setting up these schemes.
Costs and relevant data	Alternative lenders face significant costs for access to creditworthiness assessments and identity verification. Credit reference agency (CRA) data may not give lenders a clear picture of the circumstances of high-risk applicants, particularly those with little credit history or where there are gaps in CRA reporting such as rental data and non-bank income.

Working with stakeholders

5.7 Demand for high-cost credit is driven by a complex set of social, political and economic factors. It is also likely to be increased by a lack of alternatives to high-cost credit, and a lack of awareness of the alternatives that do exist.

5.8 We have engaged extensively with Government on a range of issues. We will continue to do so to help identify and put in place solutions that will aim to ensure the growth of a sustainable supply of alternatives to high-cost credit. We set out a number of specific areas where we can influence this agenda below.

Encouraging innovation

5.9 We believe action we take on high-cost credit must aim both to remove the worst harms for consumers, but also to change the market by encouraging innovation. We are seeking ways to encourage this, including opening our regulatory Sandbox to experiments aimed at developing new business models in this area that are in the interest of consumers.

35 This is the process by which money is invested in order to encourage the development of a business or market.

5.10 We highlighted in our January update that we would be willing to work with innovators to explore new and innovative approaches to responsible lending, including through the support of our FCA Innovate team and the regulatory Sandbox.

5.11 Since launching Innovate we have been working with firms seeking to provide products to consumers who might typically utilise high-cost credit, as well as firms seeking to enhance consumers' ability to budget. Some illustrative examples include:

- Oval Money – An app that helps users to build up savings by putting aside small amounts of money. These savings can then be used to pay off existing loans early. The firm worked with a consumer credit firm and a number of their customers during the test period. The intention was to assist consumers with high-cost credit to pay off their debts faster.
- Salary Finance – A socially progressive payroll-linked lending and savings platform, which plans to provide consumers with access to their earned income by the day/week. The hypothesis is that by enabling employees to access their earned income more frequently, they will be better able to manage their budget, address unexpected needs or avoid 'late payment fees' of existing commitments.
- An innovative investment model to help the responsible finance sector reach scale, through exploring whether it is possible for credit unions to invest in responsible finance providers who could then provide loans to low income consumers.

5.12 As part of this, we are keen to work with potential providers beyond the credit union sector, including banks and building societies, to discuss new ideas and innovative business models that could expand responsible lending options for consumers beyond those models currently available.

Access to sustainable capital for alternative credit

5.13 In January 2018, the Government announced its intention to provide around £55 million of funding from dormant bank and building society accounts to improve financial inclusion. It would do this by tackling issues such as problem debt and improving access to financial products and services for those on lower incomes. We noted in our January update that this may present an opportunity for supporting alternative credit initiatives.

5.14 We welcome the publication of a Statement of Intent by the Government in March. This notes that the Financial Inclusion Programme aims 'to increase the use of fair, affordable and appropriate financial products and services that boost savings, increase protection against shocks, smooth incomes and increase access to and use of fair, affordable and appropriate credit'.

5.15 We are now working closely with the Department for Digital, Culture, Media and Sport (DCMS), the Big Lottery Fund (BLF) as well as HM Treasury and the Department for Work and Pensions (DWP) to develop the Financial Inclusion Programme. This includes feeding in the findings of the research we have done, including our work on access to financial services, vulnerable consumers, our Financial Lives Survey 2017 and related behavioural research. We are sharing with DCMS and BLF our knowledge of high-cost credit and, where appropriate, other financial products to contribute to building an understanding of the market, how low income households use credit, and where there may be barriers to or gaps in access to financial services.

5.16 We will continue to support the development of the Financial Inclusion Programme over the coming months. This will include considering how to maximise the impact of the £55 million in the areas of credit, insurance and savings. We consider that the impact will be the greatest where it is used to help build and sustain initiatives which, as a result of the support, will be able to continue to promote access to, and awareness of, alternatives to high-cost credit in the future.

Key role of social landlords

5.17 In the course of this review, we have considered the degree to which demand in the RTO market may partly be driven by the social housing system and by the lack of availability or awareness of alternatives to high-cost credit.

5.18 We consider that Local Authorities and RSLs could play an important and broader role in either helping tenants directly, or in pointing them to providers that could help them get essential household goods without turning to high-cost credit. This could entail Local Authorities and RSLs increasing their roles as:

- providers of essential household goods in rented houses (as part of the rent)
- providers of credit (if appropriately authorised by us)
- a source of information about more affordable local alternatives
- brokers or introducers for specific credit firms

5.19 There are, however, a number of barriers to this happening.

Regulatory uncertainty

5.20 We have listened to stakeholders who told us that use of alternative credit works best for the financially vulnerable as part of a package of support services. They have highlighted that uncertainty over the regulatory boundary and requirements was deterring organisations, such as social landlords, from making referrals. For example, RSLs may not know what they can do to introduce their tenants to credit providers without being authorised, and they may not know what getting authorised entails.

5.21 We have prepared guidance for consultation for RSLs on the scope of regulation when they refer tenants to credit unions or CDFIs (see Appendix 2). As part of this, we have explained why we consider that these referrals are important and have made the authorisations process as streamlined and straightforward as possible. This has included creating a dedicated email address for enquiries and ensuring that there is a dedicated team to answer questions from RSLs.

Regulatory boundary

5.22 In addition, we believe there is a case to consider an amendment to the regulatory boundary to remove credit broking by RSLs from the requirement to be authorised under FSMA. Local Authorities are already excluded from this requirement for credit broking, and we believe that tenants could be helped if RSLs were able to benefit from the same exemptions as Local Authorities.

Furniture schemes operating under the Universal Credit regime

5.23 Many RSLs have told us that the guidance for social landlords on service charges in the Universal Credit regime issued by the Department for Work and Pensions has made it more difficult for them (and in some cases stopped them) from offering furniture alongside rent. Improvements to this guidance could help RSLs do more to enable their tenants to get furniture without turning to high-cost credit.

5.24 We believe there is also an opportunity, in its forthcoming green paper on housing, for the Government to consider how those moving into social housing on low income can be supported by both public and commercial organisations offering mid-cost or lower-cost credit.

Other policy developments

5.25 In the mid-term, we think there is scope to explore wider issues with Government and larger banks, building societies and credit reference agencies, including:

- how CDFIs and credit unions access credit reference agency data and the terms on which this is done
- the availability of credit reference agency data from rental information, building on the Government's recent challenge[36]
- wider access to wholesale funding for mid-cost credit providers[37]
- the range of products credit unions are allowed to offer consumers by law

Question for consultation

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

Next steps

5.26 Please respond to the consultation question (Q29) on our guidance for registered social landlords by 31 August, submitting your responses to cp18-12@fca.org.uk. Subject to the responses to consultation that we receive, we aim to finalise this guidance in Autumn.

5.27 We also encourage anyone with ideas for new business models that could help boost the supply of alternatives to high-cost credit that could be developed through our Regulatory Sandbox to contact us at sandbox@fca.org.uk.

36 In the Autumn Budget 2017, the Government announced the Rent Recognition Challenge – a £2 million Prize Fund, open to all, challenging new firms to develop new applications, or build on existing ones, to enable rental tenants to record and share their rental payment data with lenders and credit reference agencies. Further detail on the scheme can be found here: https://www.gov.uk/government/publications/rent-recognition-challenge-using-fintech-to-help-renters

37 Along the lines of the No Interest Loans Scheme operated by Good Shepherd Microfinance in Australia with support from the Australian Government (see http://goodshepherdmicrofinance.org.au/services/no-interest-loan-scheme-nils/)

Annex 1
Questions in this paper

Questions for Discussion

RTO

Q1: [For Discussion] What alternative solutions could there be to address harm from high prices?

Q2: [For Discussion] What issues should we should take into account in carrying out further work on a price-cap?

Questions for Consultation

RTO

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

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

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

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

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

Home-Collected credit

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

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

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

Catalogue credit and Store Cards

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Alternatives to high-cost credit

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

Equality and Diversity Assessment

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

Annex 2
Cost benefit analysis

Section 1: Introduction

1. FSMA, as amended by the Financial Services Act 2012, requires us to publish a cost benefit analysis (CBA) of our proposed rules. Specifically, section 138I requires us to publish a CBA of proposed rules, defined as 'an analysis of the costs, together with an analysis of the benefits that will arise if the proposed rules are made'.

2. This analysis presents estimates of the significant impacts of our proposal. We provide monetary values for the impacts where we believe it is reasonably practicable to do so. For others, we provide estimates of outcomes in other dimensions. Our proposals are based on carefully weighing up these multiple dimensions and reaching a judgement about the appropriate level of consumer protection, taking into account all the other impacts we foresee.

- Section 2 sets out our CBA for RTO
- Section 3 sets out our CBA for home-collected credit
- Section 4 sets out our CBA for catalogue credit and store cards

Section 2: Rent to own

Problem and rationale for the intervention

3. As discussed in Chapter 2 and illustrated in table 2.1, rent-to-own consumers pay significantly more than if buying equivalent products at standard retail prices. Interest rates (around 70% to 100% APR) are relatively common in the high-cost credit environment.

4. The costs are exacerbated by higher base prices, in comparison with equivalent retail prices on the same products, and "add-ons" such as insurance on theft/accidental damage and extended warranties, purchased by 90% and 70% of RTO consumers, respectively. The specific contribution of extended warranties to this cost is significant, as they typically add around 20% to weekly repayment costs although we have seen some variation in pricing across firms. These products are typically sold at the end of the sales process for the RTO agreement when consumers are overwhelmingly focused on accessing household goods which may be essentials.

5. As discussed in Chapter 2, there may be additional benefits enjoyed by consumers covered by extended warranties. For example, firms argue that extended warranties allow for faster repairs than those provided under manufacturers' warranties, that there are no fees for callouts where no fault is found, and that like for like replacements can be provided during repairs. There is an additional benefit in that it provides a single

point of contact for consumers which arguably enhances the accessibility of the warranty.

Figure 1: Comparison between manufacturer's and extended warranty sold by RTO firm

Manufacturer's Warranty	Extended Warranty[1]
Unlimited repairs including parts, labour and call-out charges	Unlimited repairs including parts, labour and call-out charges
"Reasonable time" to fix	"Fast Fix" – with specified target times but no guarantee these will be met
Replacement product "within reasonable time"	Replacement product if product can't be fixed within 10 working days
Pay a fee if there is no fault (unspecified)	No extra charge for where no fault found

6. We observe that those consumers that currently purchase extended warranties appear to derive some value from it. Data we collected from RTO firms indicated that for every £10 firms take in in premiums for these products, £4 is paid out in costs for repairs and replacements, a claims ratio of 40%. As a comparison The Office of Fair Trading (OFT) found in 2012 that claims ratios for extended warranties for domestic electrical goods had risen to approximately 50% in 2012 from 20% in 2002, but this was is still significantly lower than claim rates for general insurance which stood at 74%[1]. It is also possible that some of these claims could have been made on a standard warranty if the extended warranty hadn't been purchased.

7. Our consumer research found that some consumers had little understanding of whether these products were optional, what the services provided and their level of coverage would be without purchasing the additional warranty.

8. We consider that this proposal to ban purchase of extended warranties at the point of sale will have the effect of reducing the following harm:

- Unsuitable purchases, as consumers buy these warranties at point-of-sale with limited time to decide and possibly without due consideration of costs and additional benefits of these products.
- High costs for some consumers of using RTO where the high prices for the point-of-sale purchase of these warranties, as evidenced by the low claims ratio, increase the high overall costs of RTO offerings for consumers who are typically financially vulnerable.

9. We consider that the root cause of these harms consists of a combination of market failures, namely asymmetric information, behavioural biases affecting consumers' choices, and market power derived from point-of-sale advantage.

10. **Asymmetric information** arises when suppliers know more than consumers about the characteristics of the products. In this case, RTO firms are likely to have better knowledge of the likelihood that claims will be made on the extended warranties for the products purchased. Although firms appear to provide some standard information

1 http://webarchive.nationalarchives.gov.uk/20140402172757/http:/oft.gov.uk/shared_oft/markets-work/OFT1403.pdf

to consumers on extended warranties at point of sale it appears some consumers are not fully aware that goods typically come with standard one-year warranties, and that they could seek extended warranties elsewhere. Furthermore, RTO consumers still face uncertainty on any alternative warranties they would be able to get, and at which price. This uncertainty provides stronger incentives to conclude extended warranty agreements at point-of-sale.

11. **Behavioural biases** further increase the potential overestimation by consumers of the value of warranties[2] and can affect consumers' preferences. Two of them directly affect consumers' preferences:

- Loss aversion, whereby people suffer disproportionately at the thought of losing possession of a good, especially if recently acquired.[3]
- Fear of regretting one's decision, which further enhances the desire to protect oneself from adverse events, even if paying a price that is disproportionately high in relation to the likelihood and actual value of the good covered by extended warranty.[4]

12. The impact on consumers' choices may be exacerbated by:

- Framing of choices, orienting the focus on the relatively small impact (in pound terms) on weekly payments
- Focus on the good just purchased, physically present at point-of-sale, which reinforce the impact of loss aversion and the desire to complete the transaction and to protect oneself against adverse events.
- Persuasion and influence techniques by sellers can further suggest the purchase of add-ons as the appropriate choice.
- Limited attention and low ability to process information, which hamper the adequacy of decision at point-of-sale.

13. **Market power** arises from the point-of-sale advantage enjoyed by RTO firms which is a well-established concept in competition law and economics:

- The firm that has sold the underlying goods is the first supplier of warranties presented to the consumer and the only one present at point-of sale.
- Lower transaction costs to the firm, in comparison to competitors, as the customer is physically present to conclude the extended warranty contract and has already provided data to facilitate the credit arrangement.
- Greater convenience for the consumers, who would need to spend time to find alternative providers

2 For a more detailed discussions on the types of biases, see the FCA Occasional Paper on "Applying behavioural economics at the Financial Conduct Authority" https://www.fca.org.uk/publication/occasional-papers/occasional-paper-1.pdf

3 Kahneman, D., and Tversky. A. (1981). The Framing of Decisions and the Psychology of Choice. Science, 211, 453-458

4 Loomes, G., and Sugden, R. (1982). Regret theory: an alternative theory of rational choice under uncertainty, The Economic Journal, 92, 805-824.

- Consumers are uncertain about which alternative offers they would be able to get, and may even be unaware of the possibility to find any. We have found that extended warranty cover should be available from at least one other alternative provider.

14. The point-of-sale advantage is well documented; for instance, in the 2012 OFT Study,[5] which finds only 18% of consumers buying at point-of-sale shop around for extended warranties. It is unclear how this figure has evolved since the introduction of a new comparison website.[6] According to Fletcher (2016),[7] the website proved of limited usefulness, in particular as all but one provider only offer extended warranties linked to their own products.

15. Asymmetric information and the biases discussed above reinforce this quasi-monopolistic position as extended warranty suppliers that RTO firms enjoy at point-of-sale. We consider that consumers are not able to objectively assess the value of the additional services provided by warranties when taking into account the behavioural biases associated with purchasing add-ons and particularly at a late stage in the sales process.

Our intervention

16. We consider that banning the purchase of extended warranties at point-of-sale reinforces consumer protection and competition in terms of:

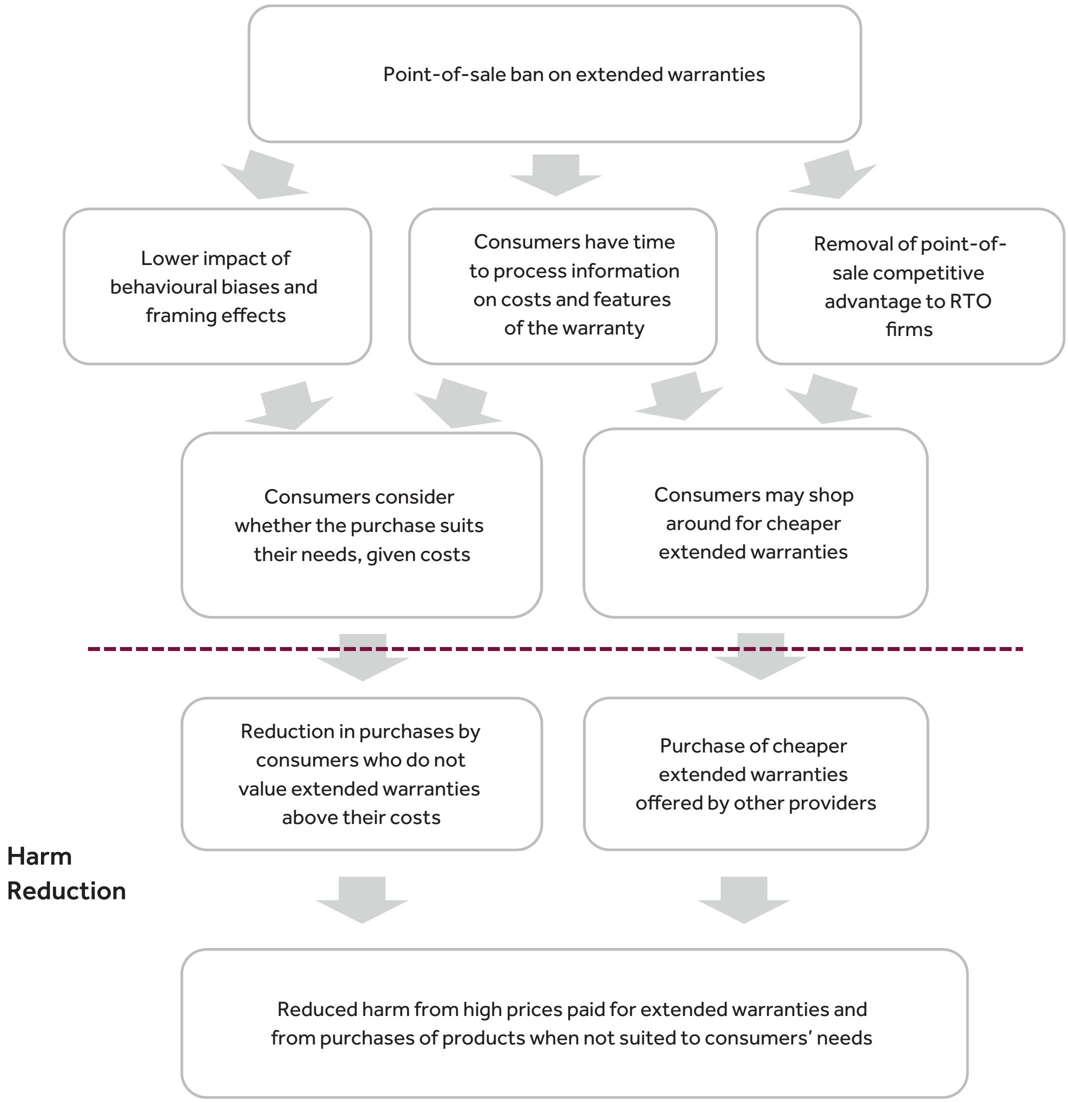
- curbing the effects of asymmetric information, as it provides a better opportunity to consumers to consider terms and conditions and hence compare the costs and the benefits of acquiring them
- reducing the impact of behavioural biases, that are more easily "activated" in the point-of-sale environment and at the time when consumers have just decided to acquire the underlying products
- removing market power from the point of sale advantage currently enjoyed by RTO providers

17. We also specify the information we expect RTO firms to provide consumers when they offer to sell an extend warranty. In particular, consumers should be given an explanation of how the extended warranty interacts with and compares against any standard manufacturer's warranty.

18. The following figure illustrates the chain of effects of our proposed intervention, leading to the intended outcome of reducing harm to consumers.

5 http://webarchive.nationalarchives.gov.uk/20140402172757/http://oft.gov.uk/shared_oft/markets-work/OFT1403.pdf
6 http://www.compareextendedwarranties.co.uk/
7 Fletcher, A. (2016): "The Role of Demand-Side Remedies in Driving Efective Competition A Review for Which?", https://www.regulation.org.uk/library/2016-CCP-Demand_Side_Remedies.pdf

Figure 1: How our intervention tackles harm to consumers



Baseline

19. Our baseline is that absent our intervention behaviour and prices would remain unchanged.

20. We note that some firms in the RTO sector do not consider that the extended warranty products they sell are contracts of insurance, but still sell them as if they are. In light of this our baseline assumes that firms are providing information on these products during the sales process that is to some extent consistent with our Insurance Conduct of Business Sourcebook (ICOBS) requirements.

21. We also note that there are obligations in the Supply of Extended Warranties on Domestic Electrical Goods Order 2005 requiring firms to provide specific disclosures to customers whenever they sell an extended warranty alongside a domestic electrical good. We assume that this information is being provided.

22. We sent a survey to RTO firms April 2018. This provided useful evidence in support of our CBA. When assessing costs of compliance, we use responses to our survey of the firms and our standard FCA cost assumptions regarding firm sizes.

23. As mentioned in Chapter 2, around 400,000 consumers hold a total value of £500m outstanding debt. Their median income is £16,100.

24. The most recently available accounting data from the firms surveyed show £40m-£45m per year in terms of revenues from sales of extended warranties around. RTO firms spend £10m-£15m per year as costs of service cover, indicating profits on the sale of warranties of around £25m-£35m per year.

25. Our proposals specify our expectations in terms of the information that consumers receive when firms offer to sell extended warranties. Our analysis of market practices indicate that the main RTO firms already provide some information to their customers on the costs of extended warranties and the services that consumers acquire when contracting them, but not to the extent of our proposed rules. There will, nevertheless, be impacts in terms of reviewing and updating existing disclosures and training staff to ensure that the new requirements are met.

Costs of our proposals

26. Our proposals entail costs in terms of:

- costs to RTO firms of compliance with new requirements including provision of additional information
- reduced convenience from changes in sale processes to those consumers who still buy extended warranties from RTO firms, but cannot do it at point-of-sale, and to RTO firms in processing those purchases at a later stage instead of straight after the purchase of the product
- loss of profits to RTO firms, as some consumers will refrain from buying extended warranties as a consequence of our intervention
- additional costs to consumers as a result of not purchasing warranties

Costs of compliance

27. Our proposals will lead firms to update their processes in order to comply with new requirements.

Updating IT systems

28. We require firms to provide key information about the costs, benefits and limitations of the extended warranty product and its interaction with the manufacturer's warranty and any insurance products sold alongside the RTO agreement. Surveyed firms indicate that IT changes to incorporate the need to check coverage and revisions to disclosure and advertising materials sum up to 30 to 50 days. Standard FCA salary assumptions on IT costs for small firms, including overheads, includes £266 daily costs to small firms, and £346 for medium firms. Considering that the market is made of small to medium firms, we assume £306 average costs.

29. The combined impact on the relatively small number of firms operating in the market should then by in the £20,000-£40,000 range in terms of **one-off costs to update IT systems**.

Familiarisation costs

30. There are approximately 10 pages of FCA policy documentation that firms will need to familiarise themselves with. Assuming that there are 300 words per page and a reading speed of 100 words per minute, it would take 30 minutes to read the document. It is further assumed that 5 compliance staff at medium firms, and 2 compliance staff at small firms read the document. Finally, the hourly compliance staff salary is assumed to be £58 at medium firms, and £42 at small firms.[8]

31. Under these assumptions, a small firm sustains £42 and a medium one £145 familiarisation costs.[9] Given the small number of firms in the RTO market, we consider that this impact is of minimal significance in proportion to the other increments in costs discussed in this CBA.

Reviewing and updating information to customers

32. RTO firms will need to review and update the information they provide to customers, following our interventions.

33. The time spent on these tasks varies depending on existing practices and the size of the firms involved. Indications from survey outcomes on the one-off impact of time to prepare disclosures point to 30 to 70 days, mostly spent by managers and directors with salaries.

34. Assuming salaries and overheads costs involved to be between £60,000 and £100,000, we estimate **one-off costs** to the industry to be in the **£25,000-£50,000** range.

Training

35. We also consider that firms will need to train employees on how to process the offerings of extended warranties to customers, both in terms of the information provided and on to engage with them once they are outside the point of sale.

36. Based on responses in relation to training of staff, we understand that, overall, some 1,100 RTO staff will receive training for 1 to 4.5 days. Combining opportunity costs of time for staff and internal providers of training, as well as payments to external providers, and including the cost of preparing training materials, results in **£0.6m-£0.9m one-off costs**.

Changes in sales processes

37. Consumers who still buy extended warranties will suffer a slight inconvenience from our interventions, as they may prefer to conclude the transaction at point-of-sale.

38. Similarly, RTO firms will face the inconvenience to process those purchases of warranties days after the sale of the underlying product, instead of immediately after

8 Standard FCA cost assumptions. In the case of hourly salary, inclusive of 30% overhead costs, they are based on Willis Towers Watson "2016 UK financial services report".

9 1/2hour x 2 compliance staff x £42 for the small firm, 1/2 x 5 x £58 for the medium firm.

it. We consider these additional costs to be minimal in proportion to the size of other costs and benefits presented here.

Reduction in profits

39. Firms may see a reduction in profits, following a reduction in sales of warranties, when consumers have more time to consider whether to buy them as a separate decision from the purchase of the underlying products. Of course these changes will also entail savings to consumers, discussed below among the benefits of the proposed interventions.

40. Our evidence mentioned in chapter 2 indicates that 70% of RTO consumers purchased extended warranties. We need to consider how these consumers' behaviour may change, in order to establish the impact on firms' profits.

41. The CBA on an intervention mandating deferred opt-in to remove the impact of point-of-sale environment in the market for Guaranteed Asset Protection (GAP) insurance estimated a likely 10% decrease in number of customers buying add-ons at the baseline price. Furthermore, "shopping around" would entail that 25% of those who buy GAP insurance do so at an alternative provider, instead of the one selling the underlying product.[10]

42. We have considered what assumptions may be appropriate for a point of sale ban on extended warranties on RTO. As mentioned in chapter 2, there is qualitative evidence of some consumers' regret in relation to sustaining the full cost of using RTO including add-ons. In addition, RTO consumers may not find it equally easy to shop around after concluding the deal on the main product with the RTO firms. On the other hand, moving the choice out of point-of-sale environment should curb the impacts of the market failures discussed above, especially in relation to how behavioural biases lead to overestimating the value of warranties. As impacts depend on these behavioural reactions, their magnitude is inherently subject to uncertainty. We have therefore applied ranges to the impacts estimated in our CBA on GAP insurance and assume a 10% to 20% decrease in the number of consumers purchasing extended warranties, and an equivalent reduction in the value of those sales[11] from RTO firms.

43. Although the proposed intervention is similar to the GAP intervention we have given consideration to the differences in circumstances, the demographics of consumers and the product being sold which all may impact how many consumers choose not to purchase these warranties as a result of our intervention.

44. For example, consumers using RTO may be more inclined to reduce their spending on insurance products as a result of a POS intervention than consumers considering GAP because their incomes are lower. This would suggest that the reduction in sales volumes would be higher.

45. However firms have told us that consumers using RTO particularly value the peace of mind that comes with extended warranties, particularly where these concern

10 Consultation Paper 14-29, p.25, https://www.fca.org.uk/publication/consultation/cp14-29.pdf. This figure was partly derived from consumer surveying.

11 Of course reductions in volume and value may differ in either direction. We do not have evidence indicating whether they are likely to be stronger or weaker for more expensive warranties, which are typically linked to more valuable products.

household goods. The claims rates on these products (£4 paid out for every £10 taken in premiums) indicates they are used by those that purchase them, and many consumers taking out RTO goods and considering the purchase of extended warranties may be existing customers who have purchased these warranties before and value them.

46. We have also considered that RTO firms may have more frequent contact with consumers than dealerships which sell GAP insurance, therefore more opportunities to conclude the sale. This means that consumers may be more inclined to conclude the sale of an extended warranty at a later date than consumers purchasing GAP insurance, where consumers may not have any further contact with the dealership once they have possession of the vehicle.

47. There are therefore many factors which may make a greater reduction in sales more likely than for the GAP intervention but counteracting factors which weigh against these. We therefore consider that the 10-20% decrease used by GAP is an appropriate starting point for assessing the cost benefit impact of this proposal. We consider that even if the intervention were more or less impactful in terms of consumers choosing not to buy extended warranties the conclusions from the CBA would remain the same. If the impact on the sale of warranties is substantially higher, this would increase the costs to firms in the form of lost profits. As the reduction in the sale of warranties would reflect consumers' choices with greater information and with an opportunity to better reflect on the decision away from the POS context, the reduced sales would also reflect higher benefits to consumers.

48. As mentioned above, accounting data show total revenues from sales of extended warranties around £40m-£45m per year, and costs of service cover around £10m-£15m, indicating profits in the £25m-£35m range. If revenues decrease by 10% to 20%, and assuming the costs of cover declines proportionately to revenue, RTO firms suffer a **reduction in profits between £2.5m and £7m per year.**

Table 1: Costs of our proposals to RTO firms

Type of cost	Industry one-off costs	Industry on-going costs
Updating systems	£20,000-£40,000	
Training	£0.6m-£0.9m	
Familiarisation	Minimal	
Reviewing and updating information to consumers	£25,000-£50,000	
Reduction in profits		£2.5m-£7m
Total	**£0.65m-£1m**	**£2.5m-£7m**

Reduction in consumers' benefits from extended warranties

49. Consumers who do not buy warranties will lose the benefits attached to them. Following the same assumptions above on the number of consumers (10%-20%) who will refrain from purchasing them, the monetary value lost will correspond to firms' reduced expenditure to provide related services, ie £1.5m-£2m.[12] We note, however, that consumers will still benefit from standard manufacturers' warranties. As they typically last one year, we assume that they will reduce these lost benefits to consumers by approximately one third. Hence the loss to consumers' benefits from extended warranties is estimated to be in the £1m-£1.33m range.

Benefits of our proposals

50. Benefits to consumers arise when their choices are less affected by asymmetric information, behavioural biases and market power from point-of-sale advantage. As a consequence:

- Consumers have a better opportunity to consider whether they are willing to pay the price to purchase the extended warranty. Those who choose not to, under the new choice architecture, benefit from saving on the purchase of a product they consider they do not need.
- Consumers also have a greater opportunity to shop around, possibly find cheaper extended warranties and save on the price they pay. We have found that extended warranty cover should be available from at least one other alternative provider, which in many cases would lead to savings for consumers, but there is a limited market for extended warranties sold by firms other than the retailer which sold the goods.

51. We have assumed above that 10% to 20% of consumers will cease to buy extended warranties offered by RTO firms. This would result in the following outcomes:

- **Savings** on purchase of warranties corresponding to lost revenues to firms: £4m-£9m per year.
- As noted above, consumers will also suffer **losses of benefits lost from use of extended warranties** corresponding to reductions in costs to firms, in the £1.5m-£2m range. As discussed in Chapter 2, we acknowledge arguments from firms that extended warranties provide a range of additional benefits to consumers above those afforded by manufacturer's warranties (eg faster repairs).
- These are partially compensated by usage of manufacturers' warranties. As they typically cover one year (versus usually three years for extended warranties), and assuming an even profile in claims against warranties over a three-year period, these would reduce the loss of these benefits to two thirds: £1m-£1.33m. **Net annual benefits to consumers in monetary terms would then be in the £3m-£7.7m range**.
- Some of these consumers may buy extended warranties from other providers, if they find offers that are cheaper than their willingness-to-pay for it.
- Of course the remaining 80%-90% consumers, who still buy extended warranties from RTO firms, are those who are willing to pay the costs involved, having time to consider how these warranties address their needs.

12 The widest potential range of reduction in consumers' benefits is £1m – £3m, but the range £1.5m – £2m corresponds to the set of assumptions that lead to the widest range in net costs to firms and net benefits to consumers.

Impacts on prices

52. In our analysis above we have shown potential reductions in the demand for extended warranties, as well as impacts on costs to firms.

53. As the compliance cost will consist of a one-off impact in adapting to changes in rules, we consider it unlikely to cause significant variations in pricing strategies by firms – unlike, for instance, what we would observe when variable costs increase.

54. On the other hand, RTO firms may react to a reduction in demand for extended warranties by changing the prices consumers pay for the warranties and/or for the underlying products.

55. The price of warranties may change in either direction:

- As consumers may find it easier to compare with alternative offers, RTO firms would need to decrease their prices to compete with other providers.
- On the other hand, price may increase if RTO firms consider that consumers who would still buy their warranties have a higher willingness to pay for them, if they are more risk averse and/or if they are more prone to use them, requiring repairs or replacement of products.[13]

56. We mentioned that extended warranties sales generate some 20% of total revenues from repayments. A reduction in extended warranties sales, therefore, may lead RTO firms to increase the prices of the underlying goods or the cost of financing to limit the negative impact on profits.

57. The profit-maximising price could in fact shift upwards, albeit not to the point of fully compensating the reduction in revenues, in a similar way as when costs of production increase. We also note, on the other hand, that consumers may react to an increase in cost of RTO offers by seeking alternative products and credit arrangements.

58. Impacts on prices will reflect the interplay between demand and supply functions for extended warranties, for credit and for the underlying products. The shape of these demand and supply functions will be affected by our interventions, as well as by other rule changes affecting alternative sources of credit. Given the intrinsic uncertainties involved, we consider that it is not reasonably practicable to establish a quantitative estimation of potential variations in prices.

Conclusions

59. Our proposals aim to reduce consumer harm as they tackle the impacts of market failures and behavioural biases affecting consumers' choices at point-of-sale.

60. Our assumption of a 10%-20% reduction in purchases of extended warranties helps illustrate the potential impacts of our intervention:

13 We consider that this "adverse selection" impact is unlikely to be significant in relation to extended warranties, as the "risk" of warranty claims is driven primarily by the quality and durability of products, rather than consumers' characteristics and behaviour.

- Reduction in profits to RTO firms: £2.5m-£7m per year.
- Net savings to consumers, considering lower expenditures and partial loss of benefits from repairs and replacements: £3m-£7.7m per year.
- One-off costs of compliance, mainly in relation to training staff: £0.65m-£1m.

61. We note that costs of compliance mostly relate to the one-off implementation of the new requirement, whereas ongoing positive impacts are sustained across the years in terms of reductions in consumers' expenditures on unnecessary or unsuitable warranties. While the estimations above are subject to uncertainties, we therefore consider that the benefits to consumers in the years following the implementation of our proposals are likely to outweigh the costs.

62. The comparison between potential costs to firms and benefits to consumers should also take into account that RTO consumers typically have low-income and difficulty to access consumer credit options offered by mainstream credit providers. As mentioned in chapter 2, median incomes of RTO consumers are estimated at £16,100 and median outstanding debt around £4,300.

63. As a consequence, reductions in expenditures may have relatively higher, positive impacts on their welfare than if savings of equal amounts were enjoyed by the average consumer.

Section 3: Home-Collected Credit

Identifying market failures

64. Our review of available evidence suggests that the market for home-collected credit can differ from what we would expect to see in a well-functioning market. These differences are summarised in the table below:

Table 1: Expectations and observed realities of the home-collected credit market

Expectations in a well-functioning market:	Observations in the home-collected credit market:[14]
Products would be well-understood by consumers, enabling them to make informed decisions.	Some consumers indicate that they are reliant on firm representatives for information, for example how much of their existing loan has been repaid.
Consumers would be aware of their options to raise additional funds from the same lender.	Some consumers are unaware that there are different ways of accessing additional borrowing from the same firm, which may be cheaper than refinancing an existing loan.
Consumers would be able to switch easily from one provider to another when engaging in further borrowing.	Some consumers are under the impression that creditworthiness checks would be more stringent, were they to apply for a loan with another provider, compared to their existing lender.
Consumers would anticipate most future liquidity needs.	Additional borrowing is highly cyclical, with a pronounced peak around the Christmas period.

14 These observations are based on analysis of CRA data and our consumer research.

Expectations in a well-functioning market:	Observations in the home-collected credit market:[14]
Consumers would initiate contact with lenders when they are in need of additional credit.	There are cases where firm representatives are prompting a conversation about the possibility of an additional cash advance, rather than consumers initiating the contact.

65. The issues highlighted in the table suggest that harm is being caused to consumers. Using the classification in *Our Mission*,[15] some consumers appear to be buying unsuitable products, and there appears to be inappropriate treatment of customers in places. As such, the highlighted issues are relevant to the FCA's operational objectives of *consumer protection* and *effective competition*.

66. These issues and the resulting harms to consumers are caused by a number of market failures, such as information asymmetries, behavioural distortions, market power, and externalities.[16] Below, we discuss how these market failures are linked to the issues in the table above.

Some existing borrowers are not fully informed about their options to obtain additional credit

67. Existing borrowers have limited information about what kind of additional credit arrangements firm representatives could offer them. Some lenders may be incentivising their firm representatives to offer the refinancing of an existing loan, as this is generally a more profitable way of providing additional credit than a concurrent loan.[17] However our consumer research suggests consumers are not generally aware that this is a more expensive way to borrow in terms of total cost. These observations suggest the presence of **information asymmetries** between borrowers and lenders.

68. **Behavioural distortions** such as present bias,[18] constraints to cognitive processing,[19] and persuasion and social influence[20] can prevent customers from choosing the best course of action. For example, the full cost of refinancing an existing loan can be obscured by the fact that the weekly payments on the refinanced loan are often the same as those of the old loan. For behavioural reasons, consumers may be focussing more on the weekly cost, as opposed to the total cost of borrowing, when making a decision about further borrowing and some appear to be unaware of how the cost of borrowing can differ between different types of further borrowing.

Further borrowing is often initiated by firm representatives, not consumers

69. There is some evidence from our consumer research that some firm representatives suggest to consumers to take out further borrowing as soon as possible, or at certain times of the year, such as Christmas.[21] The highly cyclical borrowing pattern observed

15 FCA (2017): 'Our Mission 2017: How we regulate financial services'.
16 See FCA (2016): 'Economics for Effective Regulation', Occasional Paper 13 for a description of these market failures.
17 Our recent consultation on new rules to help consumer credit firms identify and appreciate the risks their staff incentives practices pose to consumer outcomes and understand what is expected of them should be taken into consideration by firms: See FCA CP 17/20 https://www.fca.org.uk/news/press-releases/fca-publishes-proposals-staff-incentives-performance-management
18 Present bias describes the tendency of valuing immediate consumption higher than consumption at any future date. Such preferences can give rise to the undue delaying of activities that result in immediate cost, such as repaying debt, or the undue expedition of activities that result in immediate benefits, such as consumption facilitated through additional borrowing. See O'Donoghue & Rabin (1999): 'Doing It Now or Later', American Economic Review for more detail.
19 Customers can fail to make the best use of information even if it is available.
20 Particularly vulnerable customers are likely to be very sensitive to marketing techniques. In the case of home-collected credit, consumers' choices can be affected by the repeated personal interaction with firm representatives.
21 Previous studies on this subject also indicate that agents may ask consumers if they want further loans. Results of a survey submitted to us which was carried out in the early 2000s found that 40.7% of consumers surveyed reported that their most recent loan was the result of this rather than the consumer requesting a loan.

in CRA data may reflect that some borrowers are receptive to these suggestions, which would be another manifestation of **behavioural distortions**.

70. The reason that lenders could have an incentive to exploit these distortions is that, when making a decision about whether to propose additional borrowing, the profit-maximising decision does not take costs to the borrower into account. These kinds of costs to borrowers are generally referred to as **negative externalities**. Examples of these externalities include any impact on the borrowers' lifetime wealth and potential consequences of long-term indebtedness, such as mental health issues.[22]

71. To alleviate these potential negative externalities, existing regulation aims to prevent lenders from initiating conversations about additional borrowing. To the extent that firms find ways to continue such behaviours while complying with current rules, **regulatory issues** are a factor in the harms observed in the market.

Our intervention

72. Our proposals in this CP aim to improve the operation of the home-collected credit market and to address the market failures identified above. Below, the rationale for each proposal is laid out.

New information requirements for refinancing and further borrowing

73. We are proposing a new information requirement for firms when discussing further borrowing with consumers. This will require them to set out the loan options they have available to consumers when consumers initiate a discussion about further lending and the comparative costs of refinancing as opposed to taking out an additional loan.[23]

74. This remedy aims to address the information asymmetries and behavioural distortions observed in the market, by enabling borrowers to make more informed choices about which products to use for additional credit. As a result, we would expect some borrowers to shift to using concurrent loans instead of refinancing,[24] reducing their total cost of credit and non-monetary costs of indebtedness.[25]

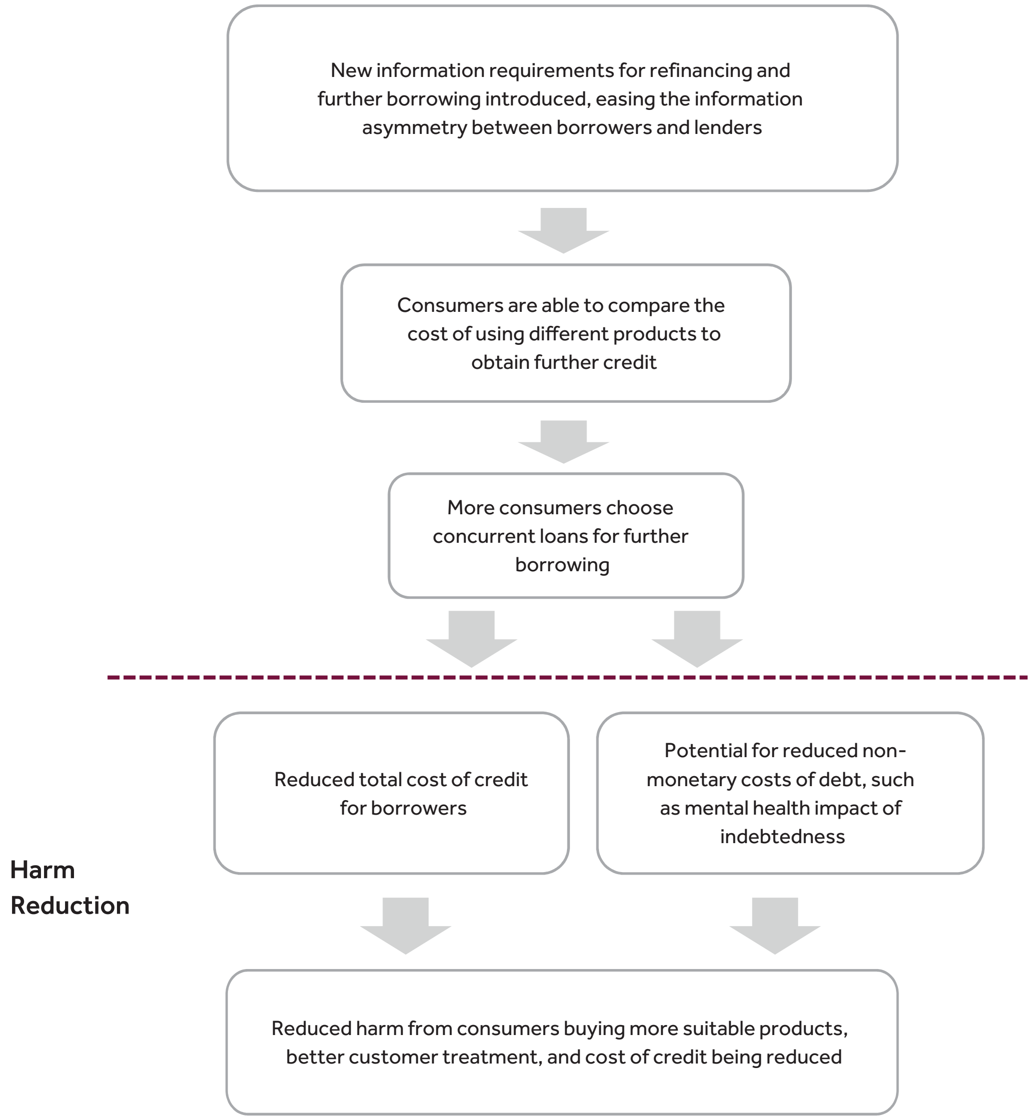
22 See Royal Society for Public Health (2018): 'Life on Debt Row'.

23 In the case of a refinancing, the existing loan is paid off by adding the outstanding principal to the principal of the new loan. In contrast, when a borrower takes out a concurrent loan, the existing loan is not paid off and both loans are instead repaid in parallel. The latter way of further borrowing typically results in a lower total cost of credit, as the principal is paid off in a more accelerated way.

24 The reason that some consumers are expected to shift is that concurrent loans are generally a less costly form of further borrowing than refinancing.

25 We have given consideration to the potential for harm from consumers taking out concurrent loans where higher weekly repayments may have the potential to cause financial distress. However we consider that the risk of this is mitigated by the requirement to assess creditworthiness and, if accepted, the consumer being able to make their own decision on what level of repayment would be affordable for them.

Figure 1: How we intend to help consumers make informed choices about further borrowing



Guidance on prohibition on canvassing off trade premises

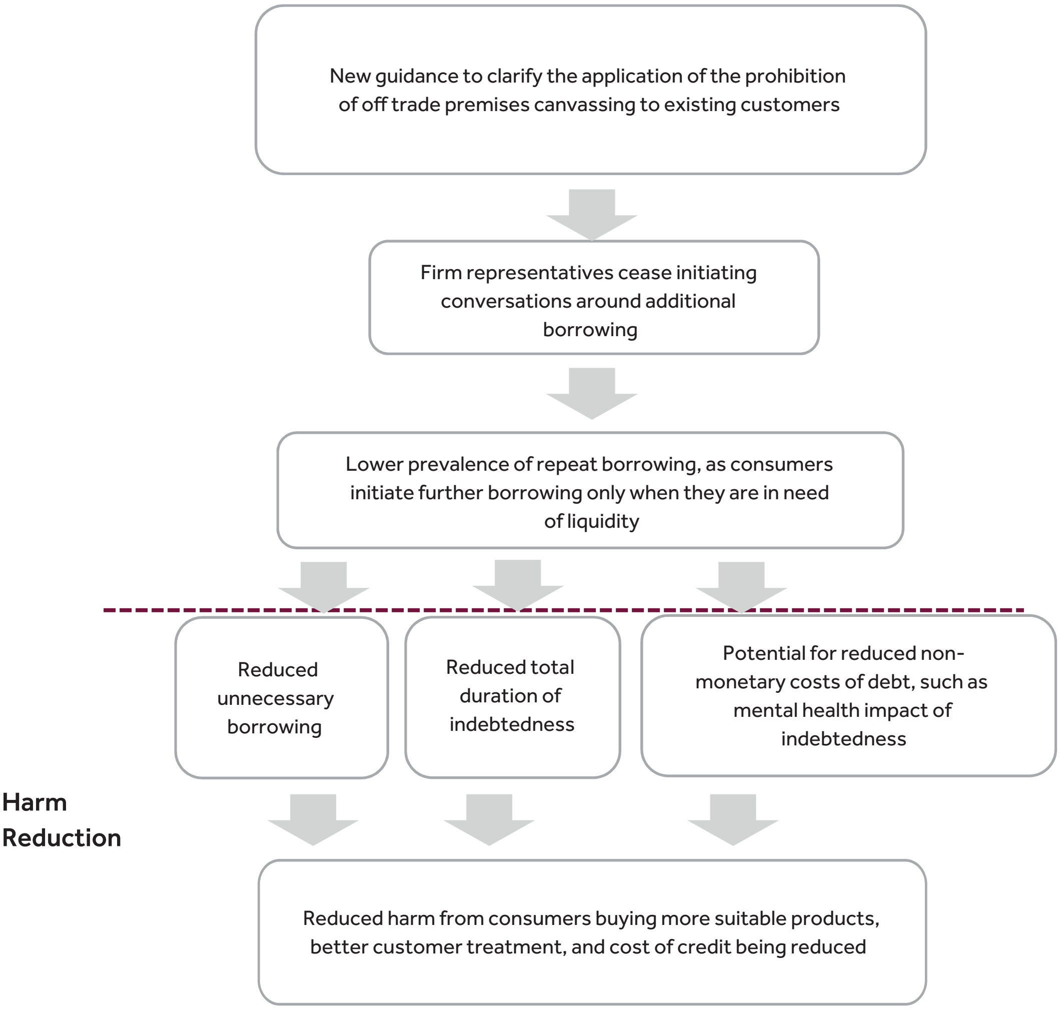
75. Section 49 of the Consumer Credit Act 1974 (CCA) prohibits the canvassing and soliciting of credit agreements off trade premises where this is not done in response to a request made on a previous occasion signed in writing. This places restrictions on firms around discussing or entering into new loans with existing customers.

76. Some firms currently address the s.49 CCA prohibition by gaining written permission from consumers when the initial credit agreement is entered into. They then treat this as an ongoing "permission to call" for the remainder of the agreement, sometimes lasting even after the consumer has paid off their loan.

77. We are consulting on new guidance to clarify the application of s.49 to existing customers, including that visits must be in response to specific requests from consumers rather than obtaining written permission at the start of the credit agreement and treating this as permission to discuss further lending on an open ended basis.

78. This measure aims to address the negative externalities of the current practice some lenders impose on borrowers and improve the effectiveness of existing regulation. In particular, in order to maximise profits some firm representatives may currently suggest additional high-cost borrowing to consumers that may not be necessary for those consumers to meet their borrowing needs. We anticipate that, in the absence of firm representatives prompting conversation about new advances, some consumers will choose to borrow only when they face an actual liquidity shortage. In this way, unnecessary reductions in lifetime wealth and mental health consequences of long-term indebtedness could be avoided.

Figure 2: How we aim to ensure that lenders cease initiating further borrowing



Measuring costs and benefits of our proposals

Baseline

79. We estimate costs and benefits against the baseline of no change in firms' practices.

Firms affected by our intervention

80. For the purposes of this CBA, we estimate the population of firms affected by the proposed rules as those firms that are authorised for either or both of the regulated activities '*Entering into a regulated home credit loan agreement as lender*' and '*Exercising*

or having the right to exercise the lender's rights and duties under a regulated home credit loan agreement'.[26] These firms are referred to as "home-collected credit" firms.

81. As of January 2018 there were 472 such firms. These are categorised into 1 large, 4 medium, and 467 small firms on a FCA-wide basis ranking of all authorised firms according to their fee block data.[27]

Data collection

82. In November 2017, we sent an information request to a sample of the largest home-collected credit firms, receiving five responses.[28] The request included questions about lending volume and value, the prevalence of refinancing, refinancing policies and procedures, and the prevalence of concurrent lending.

83. The respondents' loan volume corresponded to 62% of the total market, and the value of new loans corresponded to 64% of the overall market.[29]

84. In April 2018, we asked the same five firms to provide estimates of the resources necessary to carry out activities that would arise from the proposed rules and guidance, receiving responses from all five firms. The survey explicitly requested detail on the anticipated costs relating to the training of customer-facing staff, and IT change costs.

Generating robust estimates

85. As described above, the survey responses cover the majority of all home-collected credit loans and loans value. We therefore consider these responses to be broadly representative of the overall market.

86. To arrive at market-level estimates based on these survey responses, we assume that costs and benefits increase one-to-one with transaction volume. The industry estimates resulting from this approach are reported with a +/-10% range around the central estimate, to allow for the uncertainty arising from a survey of a portion of the market. We also present the results of another methodology in the case of IT change costs, which are likely to have a fixed component that is unrelated to transaction volume.

87. In some cases, respondents provided monetary cost estimates in addition to the requested estimates of the necessary resources.[30] In these cases, we use the firms' own monetary estimate.

26 Our proposals will affect all firms that are authorised for the activity '*Entering into a regulated home credit loan agreement as lender*'. Depending on business practices, firms that are only authorised for the activity '*Exercising or having the right to exercise the lender's rights and duties under a regulated home credit loan agreement*' may also be affected. As of January 2018, there were 15 such firms, and they are included in our calculations for robustness.

27 In particular, all regulated firms are classified using data from their annual FCA fee blocks. Each firm is allocated a rank according to where it places in a list of all firms that use the same fee block (annual income, modified eligible liabilities, etc.). Since firms often do multiple type of business, they will have a rank for each fee block they belong to. Firms are then assigned the highest rank from this set (eg if they have ranks of 9, 999, and 9999, their highest rank is 9). Firms are then ordered by their top ranking, and the absolute value of their highest ranking fee block. Once ordered, the top 250 firms are called large, firms from 251 to 1750 are called medium, and all the others are called small.

28 We selected the largest firms in order to capture the biggest possible share of the market and to avoid placing a disproportionately large burden on smaller firms in having to respond. However our proposals are designed in a way which considers the impact on smaller businesses.

29 These market shares are based on analysis of CRA data and our information request.

30 These include the necessary person-hours to make IT changes, and the number of staff that will need training.

Summary of costs and benefits

88. In this section, we summarise the costs and benefits before assessing each of them in detail.

Compliance costs

89. The two proposals would necessitate some one-off costs of complying for home-collected credit firms. These are related to firms having to train staff, making changes to their IT systems, and other adjustments.

90. We have also estimated the incremental ongoing costs that home-collected credit firms would incur as a result of making adjustments to their sales process, among others.

Table 2: Total compliance costs to the sector[31]

Type of cost	Industry one-off costs	Industry on-going costs
Familiarisation	£0.02m	
Legal review	£0.04m	
Staff training	£0.8-1.0m	
IT changes	£2.9-3.5m	
Sales process changes		£1.3-2.0m
Other	£0.02m	£0.05-0.06m
Total	**£3.7-4.5m**	**£1.3-2.1m**

Benefits

91. As a result of the proposed information requirement, we anticipate that consumers would benefit from a lower cost of credit from switching to more suitable credit products. Under the assumption that between 5% and 25%[32] of consumers change the way in which they engage in further borrowing, we estimate this benefit to be **between £3.8m and £34.2m per year**.

92. As a result of the new guidance on the prohibition on canvassing off trade premises, we would also expect some reduction in the volume of further borrowing, and associated costs of credit. The extent of this cost reduction depends on a number of uncertain and unobservable factors, such as the behavioural response of consumers, and the purpose of funds currently raised through further borrowing. As such, we are of the view that it is not reasonably practicable to estimate these benefits.

93. As a consequence of the reduced cost of credit of further borrowing, and the reduced volume of further borrowing, we expect borrowers to incur lower non-financial costs of indebtedness. These may include but are not limited to costs resulting from delaying essential expenditures to serve loans instead, and any mental health implications of struggling to repay debt.

Indirect costs to firms

94. In addition to the compliance costs summarised above, changes in consumers' behaviour resulting from the implementation of the proposals are likely to reduce home-collected credit firms' revenues.

31 Individual costs in this table may differ slightly from the reported totals due to rounding.
32 There is considerable uncertainty around consumers' reaction to policy changes. The range assumed here reflects our judgment about the likely consumer response, and the resulting estimates should be considered illustrative.

95. The extent to which firms' revenues lead to a reduction in profits depends on the degree to which firms' costs are reduced as a result of lower revenues. For example, lower levels of loan origination would be associated with lower financing costs, and lower numbers of home visits would be associated with lower operational costs.

96. The net cost resulting from a revenue reduction and cost reduction therefore depends on a number of uncertain or unobservable factors, such as firms' reduction in financing costs, and the reduction of operational costs arising from a reduced lending volume. As such, we are of the view that it is not reasonably practicable to estimate these benefits.

Compliance costs

97. In this section we estimate the direct costs of complying with our proposals. All assumptions made in this section are standard FCA assumptions, unless stated otherwise. This includes salary figures, which are based on Willis Towers Watson '2016 UK Financial Services Report' and include 30% overheads. Familiarisation costs and legal review costs of both proposals are estimated jointly, while all other costs are estimated separately for each proposal.

Familiarisation costs

98. We anticipate that there will be approximately 10 pages of policy documentation that firms will need to familiarise themselves with. Assuming that there are 300 words per page and a reading speed of 100 words per minute, it would take 30 minutes to read the document. It is further assumed that 20 compliance staff at large firms, 5 compliance staff at medium firms, and 2 compliance staff at small firms read the document. Finally, the hourly compliance staff salary is assumed to be £55 at large firms, £58 at medium firms, and £42 at small firms.

99. Under these assumptions, the one-off industry cost of familiarisation is estimated to be **£0.02m**.

Legal review

100. We also anticipate that firms will also have to conduct a review of approximately 10 pages of legal text.

101. It is assumed that 4 legal staff at large firms, 2 legal staff at medium firms, and 1 member of legal staff at small firms will review the legal text, implying a total of 5.6 hours at large firms, 4.2 hours at medium firms, and 1.4 hours at small firms for legal staff to conduct the review.[33] Finally, the hourly legal staff salary is assumed to be £64 at large firms, £64 at medium firms, and £51 at small firms.

102. Under these assumptions, the one-off industry cost of legal review is estimated to be **£0.04m**.

Staff training

103. The approach to estimate industry-wide compliance costs arising from the training of staff is to estimate the costs that the respondents to our survey would incur. We then

33 The number of legal staff reviewing the documentation by firm size is a standard FCA assumption. The estimated time required per legal staff is based on standard FCA assumptions of 28 hours per 50 pages of legal text at large firms, 21 hours at medium firms, and 7 hours at small firms. This is based on the expectation that the review is more complex at larger firms.

estimate the total industry cost by multiplying the cost to respondents by a scaling factor that reflects respondents' share of all loan originations in the industry. That is, we are assuming that firms' training costs are proportional to the number of loan originations.

104. In our survey, we asked respondents to indicate the number of customer-facing staff and firm representatives that would require training as a result of both proposed measures (ie the new rules and guidance). We also asked how long respondents expected the necessary training sessions to be.

105. To estimate respondents' cost of training, the opportunity cost of staff receiving the training is calculated based on the duration of the training and average salaries. To compute respondents' opportunity cost of sales staff time, the average hourly salary of large and medium firm sales staff are assumed to be £19 and £27, respectively.[34] One respondent noted that some business support staff would require training as well. We assume the average hourly salary of a large and medium firm business support staff to be £22 and £23, respectively. The opportunity cost of both sales and business support staff time for each respondent is then calculated as the product of staff count, hourly staff salary, and training duration.[35]

106. In addition to the opportunity cost of staff, the development and delivery costs of the training are explicitly taken into account. To estimate respondents' cost of developing and delivering training, we assume that an HR training specialist spends 40 hours to prepare one hour of training, and that the training class size is 15 staff per trainer. We also assume that the average hourly salary of an HR training specialist is £43 at large firms, and £39 at medium firms. Each respondent's cost of preparing each of the sales and the business support training is then calculated as the product of HR staff hourly salary and the training duration, multiplied by 40.[36] Each respondent's cost of delivering each training session is then estimated as the product of HR staff hourly salary, the training duration, and the number of trainings to be delivered.[37]

New information requirements for refinancing and further borrowing

107. Based on the reported staff numbers and training durations, the total training costs that respondents would incur as a result of this proposed information requirement is estimated to be £0.4m under the assumptions detailed above.[38]

108. Assuming that firms' training cost is proportional to their number of loan originations, the **industry total one-off training cost is estimated to be between £0.6m and £0.7m**.[39]

34 The set of respondents includes only large and medium firms.

35 This calculation is carried out separately for each respondent, since the training duration and salary levels differ.

36 This calculation is carried out separately for each respondent, since the training duration and salary levels differ.

37 This calculation is carried out separately for each respondent, since the training duration and salary levels differ. The number of trainings to be delivered is equal to the number of staff that require training divided by the class size of 15, rounded up to the nearest whole number.

38 One out of the five respondents provided us with a monetary cost estimate as well. We consider this estimation more reflective of that respondent's cost than our methodology, and use it as part of the total cost to respondents reported here.

39 The lower bound scaling factor used here is 1.45 and the upper bound scaling factor is 1.77. These are estimated based on the industry total of 1.7m originations in 2016 reported in FS17/2, divided by the loan volume that all five respondents indicated for the period between July 2016 and June 2017 in our information request. A margin of error of +-10% is applied to reflect the fact that there may be limits to the representativeness of our survey and information request.

Guidance on prohibition on canvassing off trade premises

109. Based on the reported staff numbers and training durations, the total training costs that respondents would incur as a result of this guidance is estimated to be £0.1m under the assumptions detailed above.[40]

110. Assuming that firms' training cost is proportional to their number of loan originations, the **industry total one-off training cost is estimated to be £0.2m**.[41]

IT changes

111. As both proposals would require firms to make some adjustments to their existing systems and processes, we anticipate that they would incur some one-off costs relating to these adjustments.

112. We estimate industry-wide compliance costs arising from IT changes by estimating the costs that the respondents to our survey would incur and then scaling by the respondents' share of all loan originations in the industry.

113. In our survey, we asked respondents to indicate the number person-hours firms expect are needed to implement the necessary IT changes. To estimate the monetary cost, we make a number of assumptions around the structure of the team that would deliver the IT change, as detailed below:

Table 3: Assumed structure of IT delivery team[42]

	Percentage of project hours	Hourly salary (inc. overheads) at large firms	Hourly salary (inc. overheads) at medium firms
Business analysis team	5%	414	366
Design team	15%	414	366
Programming team	55%	349	319
Project management team	10%	372	360
Test team	10%	349	319
Senior Management	5%	544	579

Source: Standard FCA assumptions. Salaries are based on Willis Towers Watson '2016 UK Financial Services Report' and include 30% overheads.

114. Based on these assumptions, the estimate for each respondent can be computed by multiplying the two relevant columns of each row in the table above by the respondents' reported person-hours, and then summing the resulting products.

New information requirements for refinancing and further borrowing

115. Using the methodology described above, the sum of costs for all respondents to make the necessary IT changes to satisfy this proposed information requirement is estimated to be £1.5m.[43] From this, we estimate the total industry cost by assuming

40 One out of the four respondents provided us with a monetary cost estimate as well. We consider this estimation more reflective of this respondent's cost than our methodology, and use it as part of the total cost to respondents reported here.

41 The lower bound scaling factor used here is 1.77 and the upper bound scaling factor is 1.95. These are estimated based on the industry total of 1.7m originations in 2016 reported in FS17/2, divided by the loan volume that the four respondents to our clarification indicated for the period between July 2016 and June 2017 in our information request. A margin of error of +-10% is applied to reflect the fact that there may be limits to the representativeness of our survey and information request.

42 This table shows the assumptions that are used to calculate the costs that respondents to our survey would incur, based on their reported person-hours required. No assumptions need to be made about small firms, as the respondents include only large and medium firms.

43 Two out of the five respondents provided us with a monetary cost estimate as well. We consider this estimation more reflective of these respondents' costs than our methodology, and use it as part of the total cost to respondents reported here.

that firms' IT change cost is proportional to their number of loan originations as described above.

116. When scaling respondents' costs to market-level in this way,[44] the **industry total one-off IT change cost is estimated to be between £2.2m and £2.7m**.[45]

Guidance on prohibition on canvassing off trade premises

117. Using the methodology described above, the sum of costs for all respondents to make the necessary IT changes to comply with the approach set out in the proposed guidance is estimated to be £0.4m.[46] From this, we estimate the total industry cost by assuming that firms' IT change cost is proportional to their number of loan originations as described above.

118. When scaling respondents' costs to market-level in this way,[47] the **industry total one-off IT change cost is estimated to be between £0.7m and £0.8m**.[48]

Sales process changes

119. The proposed information requirement is expected to have an impact on an average sales transaction. Based on responses to our survey, we estimate the monetary impact of the additional time taken for each transaction. We also discuss why we anticipate no such impact to arise from the proposed guidance.

New information requirements for refinancing and further borrowing

120. In our survey, we asked firms how many minutes longer an average sales transaction would be as a result of this proposed rule. When weighting answers by each respondent's transaction volume, the weighted average increase in transaction time is estimated to be 2.7 minutes.

121. With an industry total number of transactions of 1.7m,[49] this corresponds to an additional 4.5m minutes (75,000 hours) per year spent by firm representatives.

122. To compute the opportunity cost of this time, the average salary per minute of a large, medium, and small firm salesperson are assumed to be £0.32, £0.45, and £0.28, respectively. As the exact distribution of loan originations across large, medium, and small firms is not known, we use £0.28 per minute as lower bound and £0.45 as upper bound for our estimation.

44 Instead of using the origination market share of respondents to arrive at industry totals, the cost for the remaining firms could be estimated explicitly. For instance, one could assume that the average number of person-hours required for IT changes at small firms is equal to the lowest number of person-hours received from our survey of medium and large firms. The resulting industry cost of this calculation is larger but close to the range reported here. However, we consider it to be an overestimate as we expect the average small firm to incur costs that are lower than that of any medium or large firm.

45 The lower bound scaling factor used here is 1.45 and the upper bound scaling factor is 1.77. These are estimated based on the industry total of 1.7m originations in 2016 reported in FS17/2, divided by the loan volume that all five respondents indicated for the period between July 2016 and June 2017 in our information request. A margin of error of +-10% is applied to reflect the fact that there may be limits to the representativeness of our survey and information request.

46 Two out of the four respondents provided us with a monetary cost estimate as well. We consider these estimations more reflective of these respondents' costs than our methodology, and use it as part of the total cost to respondents reported here.

47 Instead of using the origination market share of respondents to arrive at industry totals, the cost for the remaining firms could be estimated explicitly. For instance, one could assume that the average number of person-hours required for IT changes at small firms is equal to the lowest number of person-hours received from our survey of medium and large firms. The resulting industry cost of this calculation is larger but close to the range reported here. However, we consider it to be an overestimate as we expect the average small firm to incur costs that are lower than that of any medium or large firm.

48 The lower bound scaling factor used here is 1.77 and the upper bound scaling factor is 1.95. These are estimated based on the industry total of 1.7m originations in 2016 reported in FS17/2, divided by the loan volume that the four respondents to our clarification indicated for the period between July 2016 and June 2017 in our information request. A margin of error of +-10% is applied to reflect the fact that there may be limits to the representativeness of our survey and information request.

49 See FS17/2.

123. Using these assumptions we estimate the **ongoing industry cost to be between £1.3m and £2.0m per year**.

Guidance on prohibition on canvassing off trade premises

124. Some firms provided us with cost information on the basis of additional time for firm representatives to depart the consumer's property with the written request and return at a later time to discuss further lending, or a "cooling-off period".

125. However under our proposed guidance firms will not have to do this in order to discuss further lending, where the firm representatives have not gone to a property to discuss further borrowing, but consumers have raised a question about further borrowing or requested further borrowing during the course of that visit.

126. If the consumer asks the firm representative to come back at a later date to discuss further borrowing, they will need to obtain the consumers written consent; but we do not see that this will lead to a material cost for firms as they can schedule this later visit at a mutually convenient time.

Other compliance costs

New information requirements for refinancing and further borrowing

127. A subset of respondents noted that they would expect to incur some one-off costs relating to changes to their post-sale information documents for consumers, and some ongoing costs relating to paper and printing of information sheets.

128. Both of these estimates provided by firms remain below £1,000 on the industry level when scaled by number of transactions, and are therefore considered immaterial.[50]

Guidance on prohibition on canvassing off trade premises

129. Some respondents noted that they anticipate one-off costs arising from setting up a monitoring process to comply with the proposed guidance.

130. When scaling to industry level, these **one-off costs are estimated to be around £0.02m**.[51]

131. Some respondents also note that they expect ongoing costs relating to additional compliance time and the training of new firm representatives to arise from complying with the guidance.

132. When scaling to industry level, these **ongoing costs are estimated to be between £0.05m and £0.06m**.[52]

50 The lower bound scaling factor used here is 1.45 and the upper bound scaling factor is 1.77. These are estimated based on the industry total of 1.7m originations in 2016 reported in FS17/2, divided by the loan volume that all five respondents indicated for the period between July 2016 and June 2017 in our information request. A margin of error of +-10% is applied to reflect the fact that there may be limits to the representativeness of our survey and information request.

51 The lower bound scaling factor used here is 1.77 and the upper bound scaling factor is 1.95. These are estimated based on the industry total of 1.7m originations in 2016 reported in FS17/2, divided by the loan volume that the four respondents to our clarification indicated for the period between July 2016 and June 2017 in our information request. A margin of error of +-10% is applied to reflect the fact that there may be limits to the representativeness of our survey and information request.

52 The lower bound scaling factor used here is 1.77 and the upper bound scaling factor is 1.95. These are estimated based on the industry total of 1.7m originations in 2016 reported in FS17/2, divided by the loan volume that the four respondents to our clarification indicated for the period between July 2016 and June 2017 in our information request. A margin of error of +-10% is applied to reflect the fact that there may be limits to the representativeness of our survey and information request.

Benefits to consumers

133. In this section, we discuss the benefits to consumers that we would expect to arise from our proposals. Each proposal is discussed in turn below.

New information requirements for refinancing and further borrowing

134. The benefits to consumers from new information requirements include a lower cost of credit of repeat borrowing through parallel loans and reduced non-monetary costs of credit.

Lower cost of credit of repeat borrowing through parallel loans

135. In what follows, the cost of repeat borrowing is estimated under the same assumptions for the cases of refinancing and taking out a parallel loan. The cost difference between those two options is then computed from these estimations.

136. In line with typical repeat borrowing transactions, we assume the following:

- In the case of a refinancing, the existing loan is paid off by adding the outstanding principal to the principal of the new loan.
- In contrast, when a borrower takes out a concurrent loan, the existing loan is not paid off and both loans are instead repaid in parallel.

137. There are two reasons why the total cost of credit is lower when repeat borrowing is carried out by taking out a parallel loan instead of refinancing, provided the timing and amounts of advances in each case are identical.[53]

138. Firstly, the principal is repaid in a more accelerated fashion when the borrower is servicing parallel loans. This is because initially the weekly payments for existing and new loans overlap, with the combined payment exceeding that under the refinancing option. As a result, the existing loan is paid off according to the original loan term. The end of the original loan term is visible as a kink in the line for concurrent loans in Figure 3 below.

139. Secondly, lenders are entitled to retain 13 days' worth of interest on the existing loan when refinancing it.[54] This retained interest results in a higher principal balance at the time of refinancing, compared to the parallel loans alternative.

140. We estimate the cost of credit difference between refinancing and parallel borrowing by calculating the amortisation schedules of each option. As the difference in cost of credit between the two options will depend on the loan term, we make these for four different maturities.[55]

141. The loans of all customers are therefore treated as four aggregated loans, with maturities of 7, 20, 39, and 52 weeks.[56] Based on the weighted-average reported in

53 In addition to the advances being the same, the total time spent in credit is assumed to be the same across both options. That is, at the time of refinancing, the term of the refinanced loan is assumed to be identical to the term of the new parallel loan.

54 We are aware that not all firms retain the full amount, but the estimates are not sensitive to this assumption.

55 In the survey, transaction volume is collected separately for loans with maturities of "< 3 months", "3-6 months", "6-12 months", and "> 12 months".

56 The maturities are chosen as the midpoints of the maturity brackets in the survey. In the case of loans reported with a term "> 12 months", the loan is assumed to be 52 weeks long.

our survey, we assume that each aggregate loan is refinanced when between 77% and 63% of the original loan is paid off.[57]

142. The interest rates that home-collected loans carry for different maturities of the average loan size were collected from the websites of 4 out of 5 of the survey respondents in April 2018,[58] and the weighted averages are displayed below with a 10% margin of error, generating a lower and upper bound:

Table 4: Estimated interest rates by maturity used for calculation

Maturity	7 weeks	20 weeks	39 weeks	52 weeks
Estimated APR (lower bound)	1,402%	553%	300%	55%
Estimated APR (upper bound)	1,713%	676%	366%	68%

143. We estimate the value of refinanced originations from the value of total originations and the share of the total number of loans that are refinanced originations.[59] This estimated value includes both the "cash-in-hand" received by the borrower and the principal used to pay off the existing loan.

144. As we do not have information on the size of refinanced loans versus loans that are not refinancing, we assume that each refinancing is the same size as the initial value of the original loan. That is, consumers are assumed to return to the same level of indebtedness at refinancing as at the time of taking out the original loan.[60] Moreover, the term of the refinanced loan is assumed to be equal to the term of the original loan at origination. It follows from these assumptions that the weekly payment of the refinanced loan is equal to that of the original loan.

145. Consumers are assumed to make no payment on either the original or refinanced loan in the period of refinancing. Therefore, one week's payment is added to the outstanding principal. Moreover, lenders are assumed to retain 13 days' worth of interest, which is added to the outstanding principal. The resulting sum is the amount required to pay off the initial loan, or "settlement balance." The difference between the value of refinancing originations and the settlement balance is the "cash-in-hand" that consumers receive upon refinancing.

Table 5: Estimated refinancing value by maturity used for calculation[61]

Maturity	7 weeks	20 weeks	39 weeks	52 weeks
Total refinancing value (estimated)	£22.6m	£117.3m	£364.4m	£108.1m
Of which "cash-in-hand" (estimated)	£6.6m	£52.9m	£157.7m	£58.5m

146. Based on these assumptions, the amortisation schedule of the refinanced loan can be calculated.

57 This is weighted both by transaction volume of the maturity and of the respondent. The range results from the +/-10% margin around survey estimates. The higher percentage is reported first, as a later refinancing means that the cost difference of refinancing and concurrent borrowing will be lower.

58 The interest rates chosen on the websites were those that had maturities close to 7, 20, 39, and 52 weeks. The rates were retrieved for loan amounts closest to the average loan size of £765 (based on FS17/2), and then weighted by transaction volume of the maturity and of the respondent. The website of the remaining respondent did not display interest rates publicly.

59 This approximation is necessary, as no data on the refinancing share of loan value is available.

60 This assumption is consistent with a typical refinancing scenario.

61 The maturity split is based on the volume of transactions for each maturity in the survey responses.

147. For taking out a concurrent loan instead of refinancing the original loan, most assumptions are the same. However, in contrast to the refinancing case, the principal of the new concurrent loan does not include an extra 13 days' worth of interest. Moreover, the weekly payments due in the concurrent case are temporarily higher than under the refinancing scenario, due to overlapping payments. After the original loan ends, the borrower only needs to serve the new loan, with lower weekly payments than in the refinancing scenario.

148. An illustrative path of the outstanding principal under both refinancing and concurrent loans is illustrated below, for the case where the consumer receives a second advance in week 26:

Figure 3: Principal balance under refinancing and under parallel loans

149. This figure shows that under the assumptions made here, the duration that the borrower stays in debt is identical in both scenarios. However, the outstanding principal of the refinanced loan is slightly higher just after the refinancing, as a result of the 13 days of interest that are retained by the lender. Moreover, in the concurrent loan case, the principal is paid off in a more accelerated fashion, reducing the total interest due. These general characteristics are not dependent on any of the detailed assumptions made above.

150. Using this methodology, we then compute the difference in total cost of credit between the two scenarios. We anticipate that as a result of the new information requirement on refinancing and further borrowing more existing borrowers will borrow using parallel loans. That is because refinancing, while being an option to raise additional cash for those borrowers that cannot afford the temporarily increased weekly payments of a parallel loan, is a costly way of obtaining new credit. In addition to affordability considerations, there are a variety of other factors that may determine the extent to which borrowing volume would shift from refinancing to parallel loans.

151. For the purposes of this CBA, we consider a range of values for the percentage of refinancing volume that shifts to new concurrent loan originations. In particular, we estimate the **change in total cost of credit that would arise if between 5% and 25% of refinancing volume were to shift**.

152. Using the methodology and assumptions stated above, we estimate the benefit to consumers from reduced cost of credit to be **between £3.8m and £34.2m per year**. The range reflects the degree of uncertainty around the behavioural response of consumers, and the margin of error around interest rates and refinancing timing.

153. In addition to borrowers changing the type arrangement they are using for further borrowing, some consumers may choose to refrain from additional borrowing when presented with a detailed explanation of the costs of doing so. Given the complex interaction of factors that would influence such a behavioural response, we consider that any such reduction in cost of credit cannot reasonably be estimated.

Reduced non-monetary costs of credit

154. In addition to reducing the financial cost of borrowing, our proposal may alleviate other potentially negative consequences of being a home-collected credit borrower.

155. Non-monetary benefits are considered challenging to quantify in general. This is compounded by uncertainty around the extent of the behavioural response that our proposed rule may give rise to. We are therefore of the view that these benefits, while potentially significant, cannot reasonably be estimated.

Guidance on prohibition on canvassing off trade premises

156. The benefits to consumers from new guidance include a lower cost of credit arising from lower levels of avoidable borrowing and reduced non-monetary costs of credit, particularly where firms are currently using open-ended umbrella requests.[62]

Reduced cost of credit arising from lower levels of avoidable borrowing

157. We expect fewer consumers to engage in further borrowing as a result of the proposed guidance. This is because existing borrowers would have to prompt firm representatives to engage in further borrowing, rather than being prompted by firm representatives. The extent of this cost reduction depends on a number of uncertain and unobservable factors, such as the behavioural response of consumers, and the purpose of funds currently raised through further borrowing. As such, we are of the view that these benefits cannot reasonably be estimated.

Reduced non-monetary costs of credit

158. We would expect a number of non-monetary benefits to arise as a result of consumers engaging in lower levels of further borrowing, of the same nature as the ones expected to arise from the proposed information requirement, as described above.

159. A recent report by the Royal Society for Public Health analyses the perceived impact on borrowers' mental wellbeing various forms of credit, including home-collected credit, can have.[63] Based on their analysis of survey evidence, keeping up with home-collected credit payments is perceived by respondents as having one of the most detrimental impacts on mental wellbeing, compared to other forms of credit.

62 We note from previous discussions with industry that some firms use different means to comply with s.49, including obtaining "permission to call" slips each time they wish to discuss further borrowing.

63 Royal Society for Public Health (2018): 'Life on Debt Row'

160. Citizens Advice notes in a recent report that home-collected credit borrowers may feel pressured to prioritise loan repayments over important other expenses, such as rent, bills, and council tax payments.[64]

161. Similarly to the proposed information requirement, as the behavioural response to this guidance cannot be predicted accurately, and as the quantification of non-monetary benefits is difficult generally, we are of the view that these benefits cannot reasonably be estimated.

Indirect costs to firms

In addition to direct compliance costs, we expect firms to incur costs that would result from consumers changing behaviour as a result of firms implementing our proposals. Each proposal is discussed in turn below.

New information requirements for refinancing and further borrowing

Lower interest revenue for firms

162. A direct consequence of consumers' reduction in the cost of credit estimated in the benefits sections above is a reduction in interest revenue for firms by the same amount. This reduction occurs, because consumers engaging in further borrowing through concurrent loans will pay back the principal in a more accelerated fashion. As a result, less interest is due on the loans than would have been on a refinanced loan.

163. However, as firms collect principal repayments in a more accelerated fashion, this capital can be redeployed earlier to loans for other borrowers. The loss in interest revenue would therefore be partially offset by reduced financing costs.

164. It is likely that at least some firms adjust the pricing structure of their options for further borrowing, in turn prompting demand changes. As the net effect of these factors depends on the decisions of individual firms and determinants of demand, we are of the view that it cannot reasonably be estimated.

Credit risk impact

165. A potential cost to firms arising from this proposed policy is that, consumers will find it harder to make the temporarily higher repayments of concurrent loans. That is, firms may receive some payments later. Therefore, they would face additional financing costs, as any late payments cannot be used to make new advances.

166. However, after consumers have paid off the original loan and only have to service the new concurrent loan, weekly payments are lower than they would have been under refinancing. Therefore, the risk that a borrower misses a payment at this stage would be reduced.

167. In addition to uncertainty around how many borrowers will choose to take out new concurrent loans instead of refinancing as a result of our proposal, it is unclear what the risk profile of these borrowers would be. We are therefore of the view that the net cost to firms of any credit risk impact cannot reasonably be estimated, but expect it to be small in magnitude.

64 Citizens Advice (2018): 'Doorway to debt'

Guidance on prohibition on canvassing off trade premises

Lower interest revenue for firms

168. As a result of the lower levels of repeat borrowing that we expect consumers to engage in, firm's revenues would decrease, though the degree of this reduction is difficult to predict.

169. The extent to which this reduction in revenues leads to a reduction in profits depends on the degree to which firms' costs are reduced as a result of lower revenues. For example, lower levels of loan origination would be associated with lower financing costs. Moreover, lower numbers of home visits would be associated with lower operational costs.

170. The net costs resulting from a revenue reduction and cost reduction depends on these uncertain or unobservable factors and as such we are of the view that these costs cannot reasonably be estimated.

Concluding remarks

171. The proposed measures are estimated to give rise to one-off costs of compliance of between £3.7m and £4.5m, and ongoing costs of compliance of between £1.3m and £2.1m.

172. The proposed measures should deliver benefits to consumers, some of which exhibit multiple signs of vulnerability[65] and whom we have a mandate to protect.

173. As a result of the proposed information requirement, we anticipate that consumers would benefit from a lower cost of credit from switching to more suitable credit products. We estimate this benefit to be between £3.8m and £34.2m per year, provided that between 5% and 25% of consumers change the way in which they engage in further borrowing. If approximately 3% of borrowers were to use concurrent loans instead of refinancing for further borrowing, the estimated benefits to consumers resulting from lower costs of credit would outweigh the estimated ongoing compliance costs.

174. We expect the proposed guidance to lead to reductions in unnecessary further borrowing and associated reductions in the cost of credit, though we consider it not reasonable to attempt to quantify these.

175. In addition to reductions in the cost of credit, we anticipate consumers to benefit from lower non-financial costs of borrowing, as a result of borrowing via more suitable means and engaging in less further borrowing. These may include but are not limited to costs resulting from delaying essential expenditures to serve loans instead, and any mental health implications of struggling to repay debt.

176. As a result of consumers incurring lower costs of borrowing, home-collected credit firms would be faced with lower levels of interest revenue. This reduction in revenues will be partially offset by a reduction in financing costs and operational costs. There may also be changes to the credit risks that firms will have to manage, though we expect the net effect of these to be minimal.

65 In particular, limited incomes, high debt to income ratios and demographic factors (see Equality Impact Assessment)

Section 4: Catalogue Credit and store cards

177. This CBA has the following structure:

- Section 1 outlines our proposed interventions.
- Section 2 presents our market failure analysis.
- Section 3 sets out our estimates of the costs and benefits with respect to Credit limit increases/interest level increases, earlier intervention, persistent debt; and credit offers.
- Section 4 outlines our analytical approach to estimating costs and benefits of the proposed interventions.

Proposed interventions

178. The proposed interventions on which we are consulting are set out in Chapter 4 of the Consultation Paper. In summary, these are:

- Intervention 1: Extending rules (already applying to credit and store cards) to catalogue firms requiring firms to:
  - Not give credit limit increases (CLI) to those at risk of financial difficulties
  - Permit customers to reduce/decline CLI offers
  - Provide a 30 day notification period prior to a credit limit increase unless waived by the consumer
  - Not increase interest to those at risk of financial difficulties
- Intervention 2: A remedy requiring firms to make clear in the pre-contractual information the consequences of failing to repay within the Buy Now Pay Later (BNPL) promotional period and to prompt their customers that the 'Buy Now Pay Later' offer is about to end.
- Intervention 3: A remedy to require firms to monitor customers' repayment records for signs of actual or potential financial difficulties (Early Intervention). Firms would be required to make reasonable efforts to contact customers identified and take appropriate action.
- Intervention 4: A remedy to encourage both firms and customers to avoid store card or catalogue debt becoming persistent, and to help customers who cannot afford to repay more quickly (Persistent Debt).

Market failure analysis

179. In this section we provide a brief description of the sector, the harm the proposed interventions are seeking to address and the underlying market failures causing this harm.

Overview of the sector

180. Catalogue credit and store cards typically work in a similar way to credit cards, except that purchases are limited to a particular retailer/ network of retailers. Consumers are given monthly statements stating account balances, interest and fees and the minimum payment required. Store cards can be used in store to make payments for goods.

181. Our analysis of catalogue and store card credit suggests that although outstanding debt is fairly large, it is significantly smaller both in absolute and proportional terms when compared to the credit card sector.

182. In 2016, 7.6 million people had catalogue credit debt on their credit file. This has increased from 7.2 million people in 2014.[66] We observe a much larger increase in the value of outstanding debt. The total value of outstanding debt has increased from £1.8 billion in 2012 to £4.0 billion in 2016. The number of customers opening new catalogue accounts fell from 2.8 million in 2012 to 1.9 million in 2016.

183. The store cards sector is much smaller than the catalogue credit sector. In 2016 1.9 million people had outstanding store card debt. The total amount of outstanding store card debt at the end of 2016 was £0.7bn. This has increased from £0.5 billion in 2012. We also see a fall in the number of consumers taking out new store cards over the period from 2012 to 2016, from 0.5 million in 2012 to 0.4 million in 2016.

184. For both catalogue credit and store cards, these data suggest that consumers are holding debt on their accounts longer than previously and they are holding higher balances on their accounts.

185. Catalogue and store card credit provide benefits to consumers by allowing them spread the cost of purchases from a specific retailer (or a network of retailers) over time. These accounts also often provide advantageous credit terms for purchases, such as interest free offers, or other rewards for using such accounts for the purchase of goods through the particular retailer.

186. There are two broad categories of firms potentially affected by the proposed rules. Up to 11 firms will be affected by the proposals. These are a mixture of traditional catalogue credit and store card providers (8 and 3 respectively).

187. In our data from credit reference agencies, we see that debt purchaser firms hold a significant amount of catalogue and store debt. Debt Purchase firms buy debt from lenders at less than its face value and attempt to collect the full balance. Debts are usually purchased for between 10p and 20p in the £, with returns expected to be twice that paid for the debt. Repayment plans are set up over longer terms, usually using standard industry Income & Expenditure forms to assess what level of payments is sustainable. We do not expect the proposed remedies to apply to or have a significant impact on debt purchasers. This is because the proportion of performing accounts

66 See FCA High-Cost Credit Review Technical Annex 1: Credit reference agency (CRA) data analysis of UK personal debt.

(accounts with non-zero balance and not a transactor) is very low.[67] This reflects that the account is usually passed on after the collections stage when the creditor has exhausted attempts with the customer to bring the account up to date.

188. Our analysis of individual sectors (ie store card and catalogue credit) is subject to the caveat that the classification of firms into the provision of each product will not necessarily be clear for firms which engage in both activities and who have not provided disaggregated figures for each type of activity.

189. We calculate the market share of each firm based on the number of outstanding agreements in the sector in 2016. In both the case of catalogue and store card credit, our survey respondents comprise the entirety of the sector.[68]

The harm we are seeking to address

190. The harm that we are seeking to prevent by the package of interventions arises from consumers buying unsuitable credit or using this credit in an unsuitable way.

191. Many consumers use catalogue credit and store cards to spread the cost of their purchases. However, a significant proportion of consumers are using catalogue and store card credit in inappropriate ways and therefore paying more interest and fees than necessary given their credit rating because of the unsuitable way they use these products. These products are not suitable for long-term borrowing as the average interest rate on catalogue and store card credit, outside of introductory offers and interest free periods, is often very high.[69] Consumers using catalogue and store card credit for borrowing over significant periods of time are likely to be paying far more than necessary for the credit (as they may have alternatives). For example, customers with long term catalogue or store card debt may benefit from paying down their balance more quickly or converting their debt to a personal loan.

192. Many consumers may be struggling to repay their debt to their catalogue and store card creditors. Sometimes this is the result of bad luck for consumer, such as job losses, that mean consumers are unable to repay their debt. It may also be because consumers take on excessive amounts of credit. Indebtedness and problems of affordability lead to a multitude of harms. There may be significant costs of debt collection and enforcement, which consumers will at least partially have to assume. These costs can be considerable, however, there are other important harms arising from problem debt. Consumers in debt are likely to suffer emotional consequences from problem debt, such as anxiety and depression.[70] Consumers may also experience harm from the impact on their relationships, and on their ability to work. Consumers in debt may also suffer from economic hardship to repay funds to creditors. For example, they may sacrifice on essentials such as food or heating to meet debts.

193. Catalogue and store card credit is purchased alongside the purchase of a good from a retailer. Consumers will, in some instances, over-purchase goods from retailers. This will mean that many purchases are made where the benefit the product provides to the consumer is less than the price paid for the good and the associated credit. The consumer would be better off not having made the purchase.

67 Non-performing accounts were little of the outstanding balances will be recouped from consumers.
68 Excluding debt purchasers and firms which have exited the market
69 Interest rates (APR) for catalogue credit ranges from 22-50%, whereas interest rates for store cards varies from 20-30%.
70 See FCA Consumer credit and consumers in vulnerable circumstances ,page 32, https://www.fca.org.uk/publication/research/consumer-credit-customers-vulnerable-circumstances.pdf

Market failures

194. In this section we summarise the relevant market failures that the proposed remedies seek to address. There are two types of market failure relevant for our proposals: information asymmetry and consumer biases.

Information asymmetry

195. Retail catalogue credit and store cards are relatively complex products and may be difficult for consumers to understand. For example, they may not understand that different purchases may be incurring different rates of interest or the implications of only repaying minimum payments on the account and the impact this has on the amount paid. Consumers may misunderstand the terms of more complex credit offers, such as buy now pay later where there will be changes in interest rate over the period of borrowing. This will be especially true for contracts where interest is backdated to the original purchase date if the total balance is not repaid at the end of the offer period.

196. Research we have undertaken shows that at least some consumers have difficulty understanding the terms of products and the implications for the way they use catalogue and store card credit.[71] Our research shows that some consumers misconstrued elements of the repayment process.

- Consumers were making minimum repayments on their store card but believing they were not paying interest.
- Consumers failed to not understanding the impact of not paying off the balance in full at the end of the interest free period.
- Consumers were unable to understand to where they were with their balance if only paying minimum amounts per month.

197. Some consumers also fail to understand they are being charged interest on their purchases.

198. These information asymmetries lead consumers to purchase goods using catalogue or store card credit without fully understanding the terms of their borrowing or the implications and cost of the repayment strategies. This will lead to many consumers significantly overpaying for credit. It will also leave them vulnerable to over borrowing and getting into financial difficulties.

199. Lenders do not have appropriate incentives to stop customers from over-borrowing and under-repaying. While, customers in default are likely to be unprofitable, customers with persistent levels of debt, or who repeatedly make minimum repayments, will be profitable for firms. Firms therefore do not have an incentive to intervene to address this behaviour unless the borrower defaults on their debt.

Consumer biases

200. Even if consumers have all relevant information, they may not make rational decisions because of the presence of deep rooted behavioural biases. In our Credit Card market study (CCMS) we undertook an academic literature review covering consumer behaviour and behavioural biases.[72] Given the similarities with credit cards and

71 PwC (2018), Usage and experiences of High Cost Credit

72 A review of credit card literature: perspectives from consumers. See https://www.fca.org.uk/publication/market-studies/review-credit-card-literature.pdf

catalogue and store card credit, we would expect the same behavioural problems to affect the way consumers purchase and use catalogue and store card credit.

201. The literature review identified the following behavioural biases that affect the credit card sector:

- Present bias – people may have excessive urges for immediate gratification, overvaluing present consumption over future consumption. As the consumer can regret such choices later, their preferences are 'time inconsistent'. Present bias can lead to self-control problems such as excessive consumption. These biases lead consumers to over-borrow which can lead to repayment problems. It may also mean consumers make minimum payments on debt leading them to pay significant amounts of interest. Present bias may also mean that consumers given credit limit increases will use this additional credit even though they would like to have restricted their own spending.

- Overconfidence – consumers are often overconfident about the likelihood of good events occurring or their own ability, including the accuracy of their judgements. For example, consumers often over estimate their ability to repay their debt, while under estimating their future spending. They may for instance assume that they will repay their debt with an offer period but not actually manage it. Consequently they incur interest they did not intend to incur.

- Framing and anchoring effects – as people have limited attention, framing and salience can determine what information is processed and how that information is processed. Even when the economic benefits of particular choices are identical in two situations, consumers may make different choices depending on how the decision problem is framed, ie, what it draws attention to. In particular, when making repayments on their catalogue or store card credit, consumers may choose to make minimum repayments simply because it is one of the options suggested by the firms. By making minimum payments, consumers will incur significant interest payments and take some time to repay debt.

202. In the CCMS we also noted a survey by Which? examining customers' understanding and perceptions of minimum repayments, which found that half of all minimum repayers (48%) thought that the minimum repayment level is recommended by their credit card provider. Such misunderstandings can lead to under repayment.

203. In our consumer research on catalogue and store cards,[73] there were examples of consumers admitting being over-confident in their ability to steadily pay off these debts. These biases lead consumers to over-borrow leading to repayment problems. This will mean they pay more for their credit than intended. Further, there was a perception amongst catalogue credit and store card customers that using these products store cards and catalogues didn't feel like using 'real money'. Because of the ability to defer the payment (at least to the end of the month), customers said they experienced the instant gratification of receiving the item(s) without needing to pay straight away. This feature and perception of catalogue credit and store cards has led some customers to spend more than they could comfortably pay off at the end of the month.

73 PwC (2018), Usage and experiences of High Cost Credit

Baseline

204. It is necessary to establish a baseline, or counterfactual, against which to assess the costs and benefits of an intervention to ensure that only those attributable to the intervention are considered.

205. While market conditions may change as the macroeconomic environment changes, we have no reason to believe that there will be a material change in the situation we currently observe in the markets affected. As we described above in the Market Overview section, the number of new accounts has fallen but the stock of existing accounts and the level of debt is growing. We therefore use the current observed market structure and levels of consumer debt within the market and we expect this position to remain the case in the future and use this as our baseline.

206. We note that the number of consumers taking on catalogue and store card accounts is falling. However, the debt held on catalogue and store cards continues to rise and therefore we assume that the population our proposals are targeted at will remain reasonably stable in the foreseeable future.

207. Implicitly our assumed counterfactual is that firms will continue their current behaviour without implementing any other changes. This is reflected by the structure of the survey, which asks firms to report costs in terms of the additional cost of complying with the regulation in excess of any currently incurred costs.

Evidence base

208. We conducted a survey of 10 firms on the potential direct and indirect costs of implementing the proposed remedies, covering all the firms we think will be materially affected by the proposals. Therefore our market wide estimates for the costs and the size of the market presented here are a simple sum of the individual firm responses.

209. This information is considered alongside account-level CRA data. The master dataset for this analysis is a representative sample of credit reference agency (CRA) data.[74] We used anonymised extracts of individuals' running credit accounts over varying periods of time to inform our assessment of the level of harm and in the assessment of benefits for our interventions.

Cross-cutting costs

210. If we make these proposed rules, we would expect firms to carefully consider rules and identify and assess the activities within their business that need to be changed to become compliant with our new rules. Neither of these activities is costless. We have estimated these costs for the firms affected using data we have collected from firms in conjunction with standard FCA assumptions.

Familiarisation costs

211. There are approximately 19 pages of policy documentation that firms will need to familiarise themselves with. Assuming that there are 300 words per page and a reading speed of 100 words per minute, it would take 0.95 hours to read the document.[75] It is further assumed that 20 compliance staff at large firms, 5 compliance staff at medium firms, and 2 compliance staff at small firms read the document.[76] Finally, the hourly

74 See FCA High-Cost Credit Review Technical Annex 1: Credit reference agency (CRA) data analysis of UK personal debt.
75 The number of words per page and the reading speed are standard FCA assumptions.
76 The number of staff reading the documentation by firm size is a standard FCA assumption.

compliance staff salary is assumed to be £55 at large firms, £58 at medium firms, and £42 at small firms.[77]

212. Under these assumptions, the one-off industry cost of familiarisation is estimated to be £2,354.

Legal review

213. Firms will also have to conduct a review of approximately 11 pages of legal text.

214. It is assumed that 4 legal staff at large firms, 2 legal staff at medium firms, and 1 member of legal staff at small firms will review the legal text.[78] It is further assumed that it will take each legal staff member 28 hours at large firms, 21 hours at medium firms, and 7 hours at small firms to conduct the review.[79] Finally, the hourly legal staff salary is assumed to be £64 at large firms, £64 at medium firms, and £42 at small firms.[80]

215. Under these assumptions, the one-off industry cost of legal review is estimated to be £3,827.

Summary table

216. Table 1 provides a high level overview of the expected costs and benefits from our proposals.

Table 2: Summary Table of Costs and Benefits

		Firms	Consumers
Credit Limit Increases	**Costs**	System costs associated with identifying consumers in financial difficulty	Denial of a CLI when incorrectly identified as being in financial difficulty
		System costs associated with informing consumers in advance of a CLI	Time spent reading notifications and contacting the firm about CLIs
	Benefits	Reduction in administrative costs of dealing with arrears and debt collection	Reduction in interest payments and late charges/fees
			Preventing the extension of financial difficulties for recipients of CLIs
			Increase in flexibility and awareness when considering CLIs
			Avoidance of emotional and psychological costs of default

77 The hourly compliance staff salaries are standard FCA assumptions based on Willis Towers Watson '2016 UK Financial Services Report' and include 30% overheads.

78 The number of legal staff reading the documentation by firm size is a standard FCA assumption.

79 The estimated time required per legal staff is based on standard FCA assumptions of 28 hours per 50 pages of legal text at large firms, 21 hours at medium firms, and 7 hours at small firms.

80 The hourly legal staff salaries are standard FCA assumptions based on Willis Towers Watson '2016 UK Financial Services Report' and include 30% overheads.

		Firms	Consumers
BNPL	**Costs**	System costs associated with providing additional information on the implications of failing to repay within the interest-free period	
		System costs associated with reminding customers that the interest-free period is about to end	
	Benefits	Reduction in administrative costs of dealing with arrears and debt collection	Reduction in revenue from sale of BNPL products, interest payments, and late charges/fees
			Avoidance of unsuitable purchases of BNPL products prompted by disclosure on the cost implications of not paying within the interest-free period
			Reduction in payments prompted by reminders that the end of the interest-free period is approaching
			Avoidance of emotional and psychological costs of default
			Reduction in negative impact on ability to borrow in the future
Early Intervention	**Costs**	System costs associated with developing a method of identifying individuals for earlier intervention	Actions incorrectly applied to an account identified as suitable for early intervention when no intervention may have been required
		Administrative costs associated with implementing remedies to help alleviate financial difficulties for individuals identified for early interventions	
	Benefits	Reduction in administrative costs of dealing with arrears and debt collection	Reduction in the likelihood/ severity of financial difficulties
			Avoidance of emotional and psychological costs of default
			Reduction in negative impact on ability to borrow in the future

		Firms	Consumers
Persistent Debt	Costs	System & IT costs associated with adapting current systems to identify individuals in persistent debt	
		Reduction in interest payments and late charges/fees	
	Benefits		Lower interest payments/charges associated with a re-evaluation of payment behaviour following intervention by the firm
			Increased flexibility of response to income shocks
			Avoidance of emotional and psychological costs of long term debt repayment

Intervention 1: Credit Limit Increases

Overview

217. Our proposed remedy would:

- Require firms to not give credit limit increases (CLI) to those at risk of financial difficulties
- Require customers are not offered CLI if have notified firm they do not want them
- Require firms to permit customers to reduce/decline CLI offers
- Require firms to provide a 30 day notification period unless waived
- Require firms to not increase interest to those at risk of financial difficulties

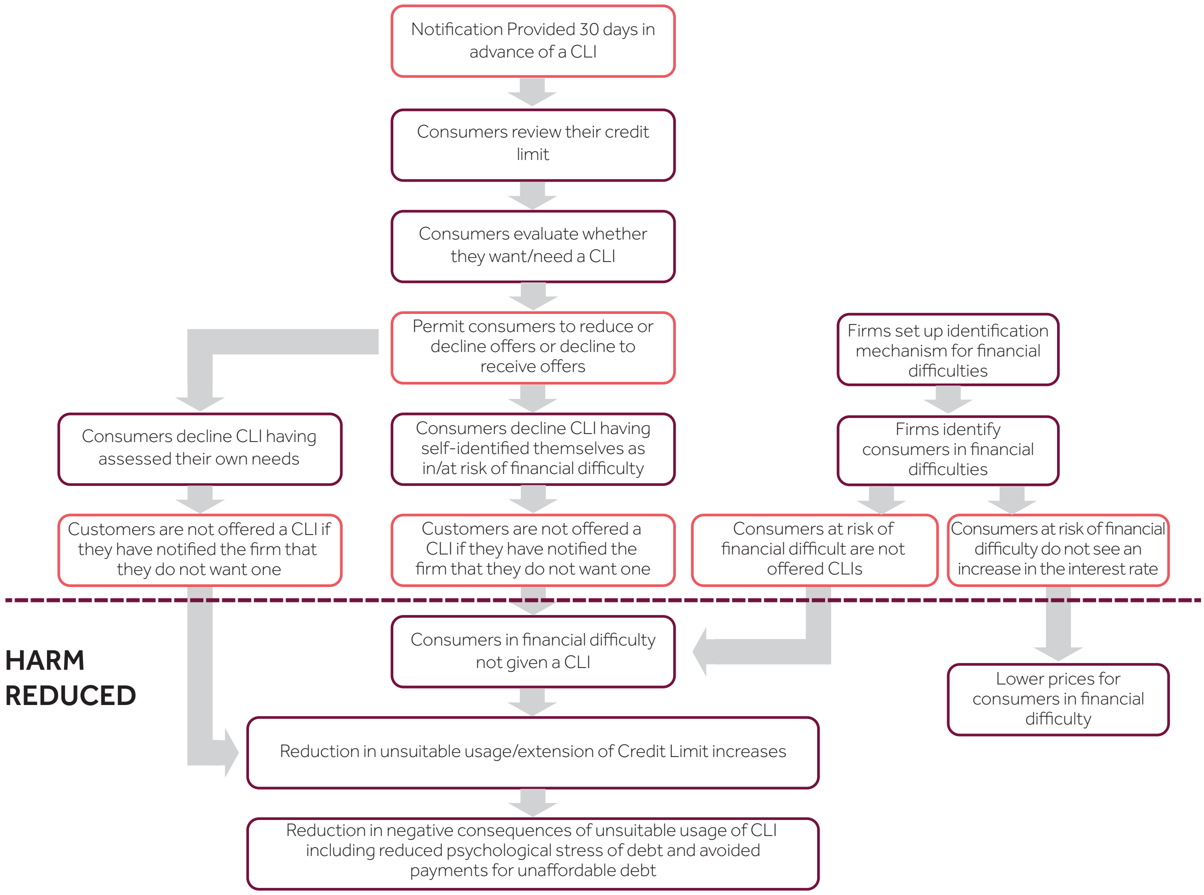
218. This represents an extension of rules which already apply to credit and store cards. As our proposals already apply to store cards, our analysis here only applies to **catalogue credit firms**.

219. This remedy aims to prevent firms from increasing the credit limit available for consumers in financial difficulties and allow consumers to avoid or reduce credit limited increases. The remedy also seeks to increase customer awareness around credit limit increases, by encouraging firms to provide notifications in advance of limit increases.

220. This remedy aims to address the harm associated with:

- The financial consequences of extending credit to individuals who are already in financial difficulties ie the exacerbation of financial difficulty.
- Consumers who are aware that they will be tempted to use credit if it is given to them and therefore over-borrow. They would therefore like to constrain themselves to avoid falling for this temptation.

Figure 2: Credit Limit Increases Proposals Causal Chain



Source: FCA Analysis – Proposed Interventions in red

Costs

221. The direct impact of the proposed remedies on firms is an increase in compliance costs associated with monitoring consumers for financial difficulties. Additional compliance costs will arise from providing notifications to consumers in advance of a credit limit increase. Most firms responding to our survey noted that they already took steps to ensure they a) did not provide CLI's where a consumer had indicated they did not want one, and b) that CLI's were not provided to consumers in danger of entering/already in financial difficulty.

222. Costs of the policy will likely arise from firms changing their systems and data usage to identify at-risk customers to prevent credit limit increases, as well as the system costs involved in informing customers in advance of credit limit increases. We expect that this notification will be part of a firms' usual communications with consumers.

223. The costs for each proposed remedy are presented below.

Ensuring customers not offered CLI if have notified firm they do not want them

Table 3: Costs for ensuring customers are not offered CLIs if they have notified firm they do not want them

	Cost Range per firm (£,'000)	Total Sector Cost (£,'000)
One-off	0 – 500	600
Ongoing	0 – 100	100

Source: FCA Analysis of Firm Survey Responses

224. Many firms noted that they already had systems in place to ensure that customers were not provided CLI's when the customer had already indicated they do not want one. Across the catalogue credit sector, the one-off cost is in the region of £600k, with a per annum ongoing cost of £100k.

Ensure that consumers at risk of financial difficulty not offered CLI increases

225. The vast majority of firms reported no additional one-off costs to this remedy, noting pre-existing systems and practices already ensure that individuals at risk of financial difficulty are not offer CLI increases. One firm did, however, report costs of approximately £100k to change their existing systems. There were no reported ongoing costs to this proposal.

Permit a customer to reduce or decline offers or decline to receive offers

226. With the exception of one firm reporting a small one-off cost of approximately £10k to alter their systems, there were no reported one-off or ongoing costs resulting from this remedy.

Notification 30 days in advance of a CLI

Table 4: Costs of providing a notification 30 days in advance of a CLI

	Cost Range per firm (£, 000)	Total Sector Cost (£,000)
One-off	0 – 300	400
Ongoing	0 – 100	200

Source: FCA Analysis of Firm Survey Responses

227. Firms typically reported small one-off costs of implementing a notification system in advance of a CLI. Total industry costs were estimated to be £200k per annum, with an industry total one-off cost of £400k.

Not increase the interest rate where the customer is at risk of financial difficulties

228. No firms reported one-off or ongoing costs for implementing this remedy, noting that this system is already effectively in place. We therefore do not address this particular remedy any further.

Indirect costs

229. We anticipate that there may be some small costs to consumers as a result of our proposals. These costs will primarily fall on consumers who are denied a credit limit increase when incorrectly identified as being in financial difficulty (for example, a consumer mistakenly identified as in financial difficulty).These costs are expected to be low: firms will have access to data and modelling which should minimise instances of incorrect freezing of credit limits, and it is in their interest to maintain a positive ongoing relationship with their customer base.

230. Further consumers will spend some time reading notifications about credit limits. Those consumers who decide to decline or amend credit limit increases will also need to spend time contacting their firm.

Benefits

Ensure that consumers at risk of financial difficulty not offered CLI increases

231. The primary impact of the policy will be to prevent the exacerbation of financial difficulties for borrowers who receive credit limit increases.

232. We estimate the benefits to consumers by estimating the interest rate savings for those in financial difficulty no longer having increased levels of credit following a credit limit increase. We also estimate the savings from avoiding late payment charges as a result of lower credit limits and the lower debt outstanding.

233. To estimate the benefits of the proposals on credit limit increase, we used an extract from the credit reference agency database. We identified all credit limit increases that occurred while an individual was 2 or more months in arrears, in the calendar year 2016. We then tracked spending behaviour in the following 6 months to assess how this credit limit increase affected consumers.

234. There are approximately 7,800 credit limit increases in the 2016 cohort where the consumer is two or more payments in arrears.[81] The credit limit increases in total increased credit limits by £1.4m, £1.2m of which was utilised in the following six months.

235. Significant numbers of these borrowers defaulted on their debts. However, £300k of this extra borrowing was not defaulted on. If consumers pay this additional debt off over a year, then they would incur additional interest of around £50k at 38% interest.[82] We might expect consumers to take longer to pay this debt off given they are in financial difficulties. If, instead, consumers take five years to pay this debt off and make only minimum payments, they pay around £230k in interest payments.[83]

236. We therefore estimate a range of interest savings of £50-230k per year.

237. Further, the consumers that do not default miss around 6,900 payments. We expect that at least some of these missed payments will be attributable to the higher amounts of debt consumers are holding. We assume that 10-20% of these missed payments are attributable to the credit limit increases. Typically these charges are £12.[84]

238. We therefore estimate that consumers could save an additional £10-20k per year from avoiding missed payment charges.

239. Additional benefits to customers will likely arise from a reduction in stress associated with being in financial difficulty in the long term.

81 There are a large number of non-significant credit limit increases in the CRA files. These appear to be technical changes in credit files and therefore do not have meaningful effects on borrows (eg credit limits move with late payment fees and interest when there is no scope for additional borrowing). We have excluded these credit limit increases from our analysis. We would expect firms to adjust their reporting to account for these types of credit limit increases and this would not affect consumers.

82 We use a weighted average APR for catalogue firms.

83 Calculated using the weighted minimum interest repayment across all firms in our sample

84 FCA analysis of firms' websites.

Notification of credit limit increases and permitting a customer to reduce or decline offers or decline to receive offers

240. We assess the remaining elements together as they collectively provide consumers greater control over their credit limit increase and amend them together.

241. Our estimates focus on consumers that would take advantage of the opportunity to reduce or decline offers because they are aware of the temptation higher credit limits may provide to overspend, and want to avoid this temptation.[85]

242. We estimate two elements of savings for consumers from the proposals. We first estimate the interest savings that consumers make on the additional purchases that they would otherwise make if given a credit limit increase. We then estimate the saving from avoiding late payment charges as a result of having lower amounts of debt.

243. There are approximately 600,000 new catalogue accounts opened each quarter.[86] From analysis of CRA data, most credit limit changes are in the first year after opening. Most catalogue accounts received at least one credit limit increase and many had more than one. We use this data to estimate that there are at least 2.8 million credit limit increases a year for new consumers in the first two years.[87,88]

244. Approximately 50% of credit limit increases were of £200.[89] While we do not know the amount of a credit limit that will be utilised, we would expect some of this credit to be used. We assume that 25-50% of this additional credit is used and that these debts are paid off over a year.

245. For the savings to consumers each year to outweigh the ongoing costs to firms, we would need at least 1% of consumers to choose to decline credit limit increases. We estimate that between 1 and 2% of consumers would request that they not be offered further credit limit increases, or alternatively that they can decline the increases. This would mean a reduction of around 28,000-57,000 catalogue credit limit increases per year.

246. Under these assumptions and analysis, we would expect consumers to avoid interest of around £300-1,100k[90] per year.

247. We know that over 30% of accounts go into arrears in the catalogue sector and will face late payment charges.[91] Typically these charges are £12.[92] We expect higher credit limits will increase the probability of incurring late payment fees. We assume consumers incur at least one late payment fee as a result of the additional debt that arises from credit limit increases. This is below what we see across all consumers and therefore (given these consumers are in financial difficulty), we might expect the true figure would be higher.

85 We note that other consumers will cancel limit increases to gain some peace of mind benefits. We do not estimate these benefits.
86 See Technical Annex
87 We assume that those consumers affected by CLIs whilst in financial difficulties do not choose to amend their CLIs
88 Noting this will under estimate credit limit changes for older accounts.
89 FCA analysis of CRA data
90 Interest payments are calculated as the difference between the implied payment schedule and the original value (£1.68m-£1.42m) for the lower-bound. Additional late payments are calculated as the number of CLIs multiplied by the proportion of late fees (20%) times the size of the late fee (£12) ie 28,000*12*0.2 =0.07m for the lower-bound. Adding these two values together produces a total saving of £0.3m per year
91 See Technical Annex
92 FCA analysis of firms' websites.

248. Given these assumptions, we estimate that consumers would avoid late payment fees of approximately £70-140k per year as a result of these proposals.

249. We would also expect consumers to avoid the associated costs and charges levied by firms to cover the costs of debt collection and enforcement, and the additional interest which may be charged on late payments.

250. We note that the benefits to consumers described above are, in the most part, transfers from firms to consumers. We expect other benefits to consumers to arise from these changes but we have not been able to estimate them. Consumers whose credit limit increases are declined will gain peace of mind and some will also avoid the emotional and financial costs of arrears and defaults, such as the costs associated with collection activity.

Table 5: Annual savings to consumers in interest fees and charges

	Consumers saving in interest per year, £'000s	Consumers saving in late payment fees pear year, £'000s	Total savings per year, £'000s
Ensure that consumers at risk of financial difficulty not offered CLI increases	50-230	10-20	60-250
Notification of credit limit increases and permitting a customer to reduce or decline offers or decline to receive offers	300-1,100	70-140	330-1,190
Total benefits to Customers	350-1,330	80-160	390-1,440

Note: Due to rounding these figures will not add up
Source: FCA analysis

Benefits to firms

251. We expect the credit limit increases proposals will reduce the administrative costs for firms of dealing with arrears and debt collection which are charged off by reducing the probability of individuals in financial difficulties increasing the size of their debt. We also expect a reduction in the long term costs associated with reduced late payments from individuals in financial difficulty and who currently might receive credit limit increases. This could be either through consumers limiting their own credit or for those at risk of financial difficulty. Firms will experience a reduction in interest payments on later charges/fees. However, we expect the overall reduction in probability of customer defaults and the defaulted debt which is costs to recover (if at all), may mean there will be some benefits for firms.

Conclusion

252. Overall we expect our remedies to be net beneficial overall. Firms have typically reported very small compliance costs across all elements of the remedy. We only need to see a small change in consumer behaviour for the savings to consumers to exceed the compliance costs. Additionally the benefit to firms in the forms of reduced debt collection costs and reduced probability of default, which we have not quantified, will add to this net benefit.

Intervention 2: Buy Now Pay Later and similar offers

Overview

253. This remedy aims to prevent customers from entering financial difficulties by requiring firms to improve their disclosure of complex credit offers such as Buy Now Pay Later schemes to improve customers understanding of the products they are purchasing.

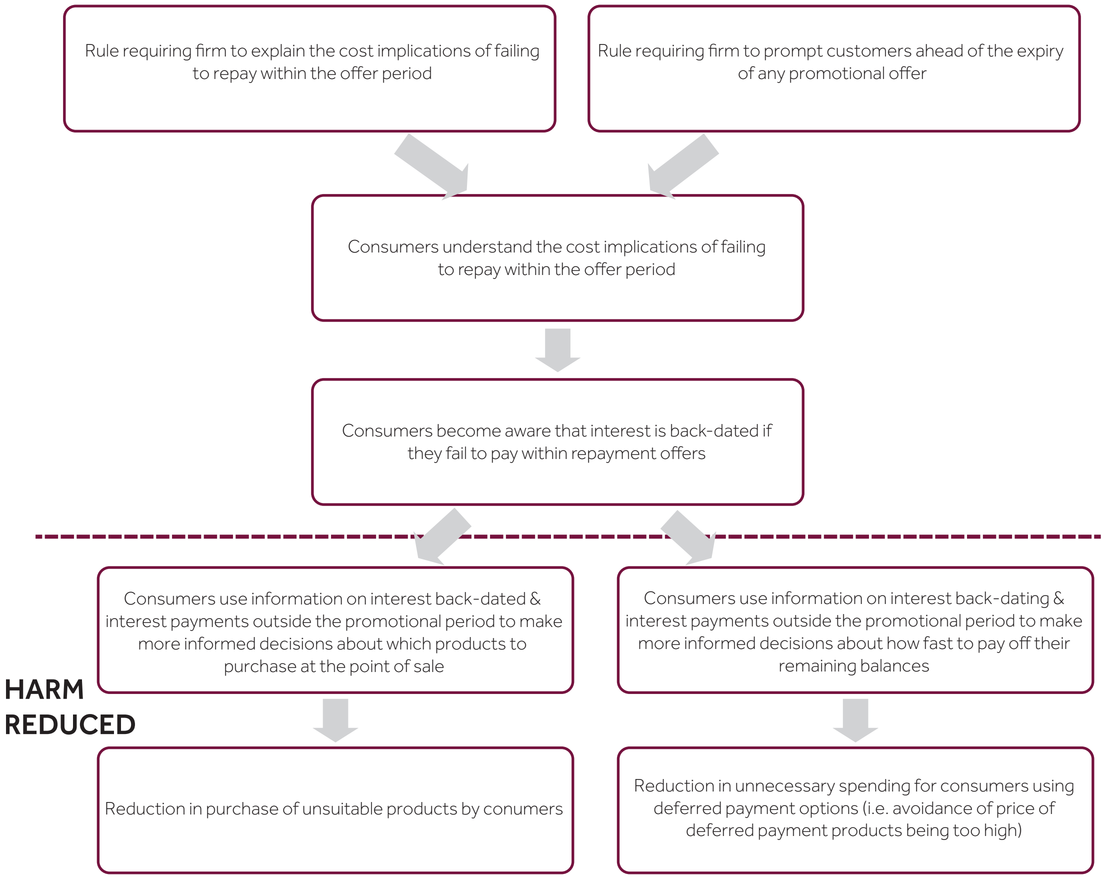
254. Our proposed remedy would:

- Require firms to disclose the cost implications of failing to pay within the offer period
- Require firms to prompt their customers (separately from the monthly statement) that the 'Buy Now Pay Later' offer is about to end and that interest will be charged if the customer does not repay within the BNPL offer period.

255. This remedy aims to address the harm associated with:

- Unsuitable purchases motivated by customers lack of understanding of back-dated interest (applying interest on outstanding balances at the end of the interest-free period covering the period back to the original purchase date of the product) if they fail to pay within repayment offers.
- The financial consequences of missing repayments, for example late/default fees and the subsequent extra interest that may be charged on the late payments.

Figure 3: Complex Credit Offers Proposals Causal Chain



Source: FCA Analysis

Costs

256. The primary direct impact of implementing the Buy Now Pay Later (BNPL) remedies will be an increase in administrative costs associated with providing additional information associated with the interest charge from failing to fully repay during the repayment period, and a prompt to remind customers to pay by the end of a promotional period. The majority of firms surveyed indicated they did not engage in BNPL promotions, and as such would incur no cost from the proposed remedies.

257. For the remaining firms, firms will incur systems costs to ensure that consumers are given information about the cost implications at purchase and prompted to consider that their offer is about to end. The firms that operate online will mainly have systems change costs, while those who also sell through retail premises will have to train staff. Further, purchases will take slightly more time to complete.

258. We do not separately identify store cards in this section as only one firm offers Buy Now Pay Later and therefore would incurs costs from these proposals.

259. The costs for each proposed remedy are presented below.

Providing additional information to customers on the cost implications of failing to repay within the offer period before an agreement is finalised

Table 6: Costs of providing additional information to customers on the cost implications of failing to repay within the offer period before an agreement is finalised

	Cost Range per firm (£,000)	Total Sector Cost (£,000)
One-off	0 – 100	200
Ongoing	0 – 200	300

Source: FCA Analysis of Firm Survey Responses

260. Of those firms using BNPL schemes, the reported one-off compliance costs from providing additional information typically arise from a combination of system changes, training costs, and the associated administration costs of actually sending out the additional information. We estimate the total one-off costs of these activities are £200k.

261. Similarly, the ongoing costs primarily come from resources such as phone management and marketing teams. The total sector cost per annum is estimated to be £300k per annum.

Providing a specific prompt to customers to remind them of the need to repay before the expiry of a deferred repayment offer

Table 7: Costs of providing a specific prompt to customers to remind them of the need to repay before the expiry of a deferred repayment offer

	Cost Range per firm (£,000)	Total Sector Cost (£,000)
One-off	0 – 100	100
Ongoing	0 – 100	100

Source: FCA Analysis of Firm Survey Responses

262. Catalogue firms did not report any ongoing costs from this proposal, with only one firm reporting one-off costs of approximately £100k to adapt pre-existing prompt systems. Ongoing costs, for store card firms, were typically associated with marketing team costs and the cost of administering the prompt itself. These costs when scaled to the industry were approximately £100k per annum.

263. There will be costs to firms from the lost revenue from consumers paying debt back more quickly (and within the interest free periods) or not making purchases at all. This will be partially offset by an increase in recoverable debt: provided consumers understand the additional disclosure and make an informed decision to purchase the product, those customers who are charged back-dated interest will be aware in advance, and may be more financially prepared to deal with this issue compared to the current population of borrowers.

Benefits

264. Consumers who are caught out by buy now pay later products will end up paying more for products than they originally expected. Consumers will benefit from our interventions by a reduction in mistakes in their purchasing decisions and in the way they pay down the debt.

265. We note that there are two broad types of product in this sector: backdated and non-backdated products. We expect there to be benefits to consumers of both types of products, however, this benefit is expected to be larger for backdated products.

266. We estimate two elements of benefits we estimate.

- Consumers may avoid making purchases that they would be choose not to make if they had a better understanding of the credit product. Alternatively they would still buy the product but would use cash or a better value alternative source of credit for the purchase.
- Consumers make the same purchases but the prompts at pre-purchase and before the end of the offer period mean consumers avoid interest payments that they did not expect or plan for.

267. We estimate the benefits from consumers either not purchasing the product or changing their repayment schedule ie repaying in full before the end of the interest-free period.

268. In our survey of catalogue and store card firms, we asked firms a number of questions about the number of customers using deferred payment (or similar) options, the value of these purchases, and the length of time it takes consumers to fully pay off their balances

269. According to our survey of firms,

- there are 2.7m consumers who currently use these products.
- Of these, 1.2m fail to pay the balance back in full before the introductory period ends.
- The average balance they hold at the end of the introductory rate is £219 and they hold this debt an additional 8 months on average.

Providing additional information to customers on the cost implications of failing to repay within the offer period before an agreement is finalised

270. We estimate the interest savings for the consumers who avoid making purchases because of the pre-contract disclosure. While the consumer also avoids the cost of the product, this is balanced against the original demand of the consumer for the product ie they were willing to purchase the product in the first instance. Therefore by not purchasing the product the consumer has lost out on a product they wanted to buy, but have benefitted by not paying the additional interest payments.

271. We have estimated the proportion of consumers that respond to the proposals. Our experience of disclosure remedies suggests we would expect relatively low response rates.[93] We anticipate higher rates of behavioural changes (ie not purchasing the product or altering repayment schedules) for disclosure on schemes which backdate interest. Since backdating interest will result in greater interest payments, this assumption means more consumers alter their behaviour when the potential loss is higher. For simplicity we assume a fixed proportion of consumers respond to each remedy, taking a lower and upper-bound of and 0% and 5% for non-backdated interest products and 1% and 10% for backdated products respectively.

272. For those consumers that no longer make the purchase, we assume that the benefits are all the interest payments the consumers would otherwise have made on the purchase.[94]

273. We estimate this benefit to be between £0.3-3.0m[95] focussed on backdated interest products.

Providing a specific prompt to customers to remind them of the need to repay before the expiry of a deferred repayment offer

274. We estimate the interest savings for those consumers that, as a result of the prompt prior to expiry, avoid unexpected interest payments due to repaying their debt in the offer period. We estimate the benefit as difference between the original value of the product (paying the product off in full before the end of the promotional period) and the estimated total amount paid absent the intervention (including interest payments after the interest-free period).

275. We assume that the prompt 1 month prior to the end of the interest-free period causes those who respond to pay off any remaining balance prior to the end of the interest-free period. For consistency with our earlier assumptions, our lower-bound estimates assume 1% of consumers alter their behaviour as a result of the disclosure, while our upper-bound assumes 10% of consumers change their repayment.

93 For example, in Occasional Paper 5, a disclosure remedy making consumers aware of potential savings elicited a 3.2 percentage point increase in consumer shopping around and negotiating See FCA Occasional Paper 5, 'Encouraging consumers to act at renewal', see https://www.fca.org.uk/publication/occasional-papers/occasional-paper-12.pdf

94 We also assume that the typical interest-free period is 6 months in length, and that consumers pay off their debt in fixed monthly instalments. These instalments vary in size depending on whether or not the consumer is in the interest-free period or not ie there is a fixed payment corresponding to the interest free period, and a different fixed payment outside the interest free period. We use the individual firms' APR interest rate to calculate the interest payments made.

95 We assume that consumers were initially willing-to-pay at least the original value of the product. We also assume that the unforeseen interest payments (interest accrued from backdating) is the loss to consumers.

276. We estimate the interest savings to be between £0.4-4.4million[96] across both backdated and non-backdated products.

Table 8: Benefits to consumers per annum of increased clarity of credit offers

	Providing additional information to customers on the cost implications of failing to repay within the offer period before an agreement is finalised	Provide a specific prompt to customers to remind them of the need to repay before the expiry of a deferred repayment offer
Annual Benefits to sector (£mil)	0.3 – 3.0	0.4 – 4.4

Source: FCA Analysis of Firm Survey Responses & desk-based research

Conclusion

277. Overall the policy recommendations for complex credit offers appear to be net beneficial. Firms have reported minimal (less than £0.5 million in aggregate) one-off and ongoing costs to implementing both of the proposed remedies. Even in our lower–bound projected estimate of benefits, both disclosure at the point of sale, and just prior to the end of the promotional period produce benefits of over £0.7 million by themselves. The change in consumer behaviour resulting from the prompts would therefore not need to be significant for the benefits to exceed the costs of these proposals. Given our experience of previous disclosure remedies, we would expect this threshold to be met.

Intervention 3: Earlier Intervention

Overview

278. This remedy aims to prevent customers from entering financial difficulties by encouraging firms to not only identify potentially at-risk customers earlier but also to take action where possible. As with our interventions on credit cards, we expect there to be incentives for firms to prevent customers from defaulting, and an ability for firms to identify potentially at-risk catalogue and store card credit customers prior to them entering financial difficulties.

Proposed Remedy

279. Our proposed remedy would:

- Require firms to monitor available data to identify customers either at risk of or in financial difficulties.
- Require firms to establish and maintain appropriate policies for dealing with customers at risk of financial difficulty.

280. We do not prescribe a particular methodology for firms to use when either assessing if individuals are at risk of financial difficulties, or the subsequent intervention method.

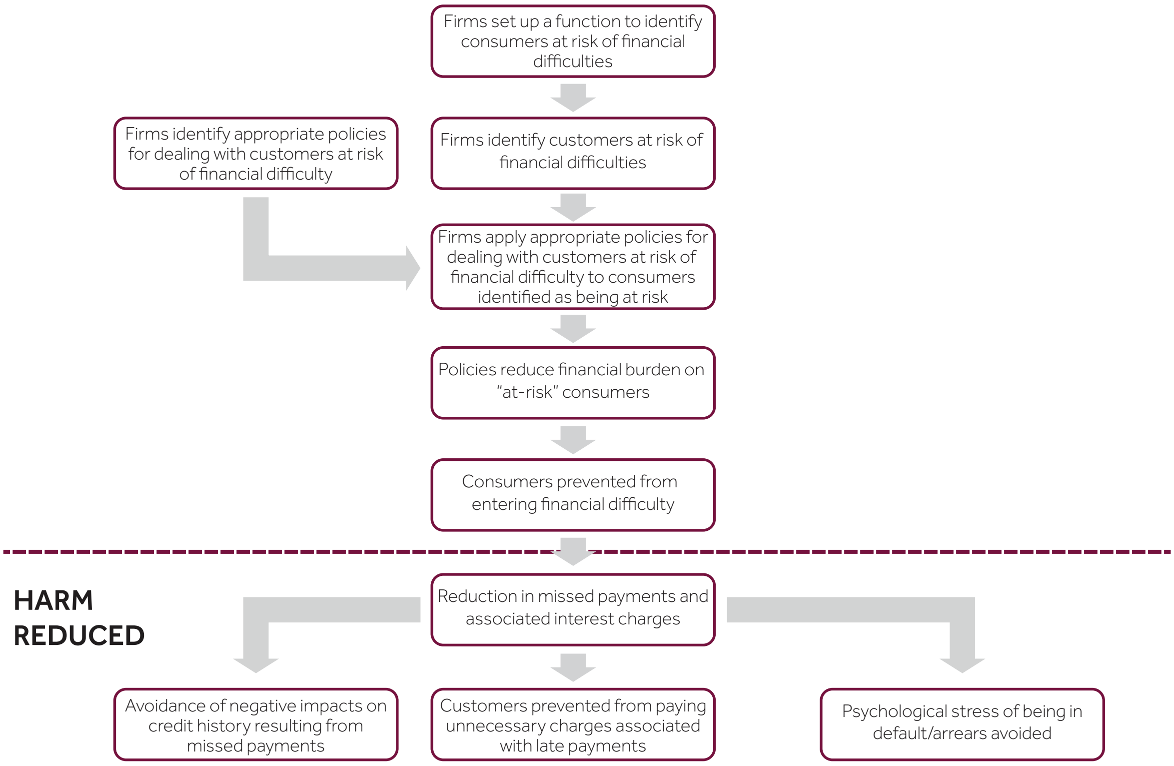
96 We take the difference between the balance remaining at the end of the interest-free period and the implied total amount the consumer would pay absent the intervention. This difference provides the average benefit per firm. We then scale by the number of consumers per firm, and use our 1% and 10% assumptions to generate lower and upper-bound estimates of the benefit. Eg a consumer with an implied total payment of £600, with a remaining balance of £220 at the end of the interest-free period would see a benefit of £380. We then scale this figure by the number of consumers and the proportion we expect to repay earlier as a result of the intervention

Firms will be best placed to consider these approaches based on their own knowledge of their data and customer portfolio

281. This remedy aims to address the harm associated with:

- The financial consequences of missing repayments, for example late/default fees and the subsequent extra interest that may be charged on them.
- Personal distress caused to customers who are in arrears/default
- The consequences of default for a subset of customers which may lower credit score and lead to an increased inability to borrow.

Figure 4: Early Intervention Proposals Causal Chain



Source: FCA Analysis

282. Our proposal requires firms to take appropriate action where there are signs of actual or possible financial difficulties in relation to a catalogue credit or store card customer.

Costs

283. As with our previous work on credit cards, we expect the direct impact of the earlier intervention remedies to be an increase in administrative costs to firms from monitoring customers for potential financial difficulties. As with credit cards, we found that the majority of firms already had systems in place to monitor borrowers at risk of defaulting; suggesting the industry cost of implementing the remedy will be low.

284. Costs of the policy will likely arise from the costs firms face from changing their systems and data usage to identify at-risk customers at an earlier stage, as well as the costs of implementing potential actions to help alleviate financial stress on at-risk customers (eg freezes on late fees or interest payments).

285. The costs of identifying individuals at risk of entering financial difficulties, as well as developing, maintaining, and implementing appropriate actions to help those consumers are recorded below:

Table 9: One-off costs of identifying individuals at risk of entering financial difficulties and taking appropriate actions to deal with them

	Cost Range per firm (£, 000)	Total Sector Cost firm (£, 000)
Catalogue	0 – 100	300
Store Card	0 – 100	200
Total	0 – 100	400

Source: FCA Analysis of Firm Survey Responses

Table 10: Ongoing costs (per annum) of identifying individuals at risk of entering financial difficulties and taking appropriate actions to deal with them

	Cost Range per firm (£, 000)	Total Sector Cost (£, 000)
Catalogue	0 – 300	500
Store Card	0 – 300	500
Total	0 – 300	1000

Source: FCA Analysis of Firm Survey Responses

286. Firms typically reported aggregated costs for this intervention ie the combined cost of identifying and dealing with customers at risk of entering financial difficulty. Those that reported disaggregated figures indicated that the bulk of costs came from the one-off changes to their system to identify individuals in danger of falling into financial difficulties.

287. The estimated one-off compliance costs are approximately £400k, while the ongoing compliance costs per annum are estimated at £1 million. These ongoing costs tended to support an ongoing enhancement in data collection and the costs of maintaining and updating models used to identify potentially at-risk consumers.

288. Additionally, indirect costs may arise to firms through customer relationship damage, through intervening with a customer's credit via the early intervention mechanism when it may not have been necessary to do so. This will also partially fall on the customer if it results in a reduction in credit available.

Benefits

289. The primary impact of the policy will be a reduction in the number of borrowers who enter financial difficulties and a reduction in the severity of these financial difficulties.

290. There are many possible ways in which a firm could change the way they interact with consumers in financial difficulty. As an example of a policy a firm could implement as part of the early intervention process, we have assumed the firm takes action by applying a fee freeze on accounts that have been identified as suitable for early intervention.

291. To estimate the benefits from such a fee freeze, we identify consumers who have missed 2 or more payments on another product.[97] This is an indicator a consumer that might require early intervention. We note that approximately 60%[98] of those identified as potential candidates for early intervention subsequently miss payments on their store card/ catalogue credit account within a 6 month window.

292. A fee freeze here means that a consumer avoids any late fees associated with missing a payment. As with credit limit increases, we assume late fees are £12. We apply fee freezes to accounts for 6 months following being targeted for early intervention.

293. To account for the fact the firms will not be able to perfectly predict which individuals will require intervention based on the early intervention flag, we divide individuals into those who would have benefitted from early intervention, and of those who would not require intervention. We then take a random sample of each of these groups. The benefit of those who require intervention will be traded off against accidentally removing late payment fees for individuals who were not in need of early intervention.

294. We assume 80%-90% of individuals requiring early intervention have the fee freeze applied. We also assume that 5-10% of those not requiring intervention receiving an accidental fee freeze. This enables us to create a range of the potential benefits.

295. We think these are plausible assumptions but it is not possible to accurately predict the outcome from the policies that firms develop. We might expect that firms would design systems to ensure that only a very low proportion of individuals who are not in need of early intervention receive it. We also expect that given the amount of data they hold on consumers, firms should be able to identify consumers in need of early intervention with reasonable accuracy.

296. This example identification and intervention mechanism yields benefits of approximately £7.0-£8.0 million per annum.

Table 11: Benefits per annum of example early intervention remedy

	Benefit (£m)
Catalogue	6.1 – 7.0
Store Card	0.8 – 0.9
Total	7.0 – 8.0

Source: FCA Analysis of CRA data

297. While we have partially adjusted[99] these figures for transfers from firms to consumers by accounting for mistaken fee freezes, the estimates provided will still include transfers from firms to consumers. We note however that a proportion of the fees avoided by consumers when the proposals are applied are a true benefit. This benefit arises from better managing the consumers in financial distress and therefore avoiding some of the associated financial and non-financial costs of debt distress. However, the

97 We use a 10% random sample of the CRA dataset for store card and catalogue products in 2016 to estimate the potential benefit of applying a system of early intervention. Based on the CRA data, there are approximately 9.7 million active agreements across catalogue and store card credit (8.3 million and 1.4 million respectively) .For the sake of exposition of the potential benefits, we utilise information available on the number of missed payments on other products (neither store card nor catalogue) as an example for determining early intervention action on catalogue and store card credit.

98 Analysis of CRA data

99 This adjustment process is as follows: we take the benefit of the fee freeze to consumers who would benefit from intervention, and subtract the value of fee freezes for those accidentally offered a fee freeze.

remainder of the fee represents a transfer from the firm (who has now forgone the late fee) to the consumer.

298. These benefits are primarily in the catalogue credit sector (approximately 88% of the benefit falling on the catalogue credit customers). This primarily reflects the fact that 81%[100] of the products under consideration were classified as catalogue credit, with the remaining difference reflecting a higher proportion of missed payments for catalogue products relative to store cards.

Other benefits

299. Indirect benefits to customers will likely arise from a reduction in stress associated with being in default/arrears, as well as a reduced impact on credit score and ability to borrow in the future. We do not believe it is reasonably practicable to estimate these indirect benefits.

300. We also expect there to be a lowering of costs associated with late payments and recovering late debt as a result of the policy. While interest revenue will decline, firms will have lower levels of outstanding lending, and should benefit from a lower probability of customer default.

Conclusion

301. The implementation of an early intervention identification and action system appears to be net beneficial. Firm's one-off and ongoing costs represent an aggregate sector impact of less than £1 million in terms of one-off and ongoing costs per annum. Benefits of implementing fee-freezes alone significantly exceed this, with the 2016 cohort of the CRA dataset indicating benefits in the region of £7 million. We note that in addition to the fact that firms may apply other policies alongside limited fee freezes (likely further increasing the benefit to consumers), the precise data and internal risk models firms have access to will likely lead to more efficient methods of early identification than we have modelled. As such we expect the indicated benefits to be a lower bound on the potential impact of the policy.

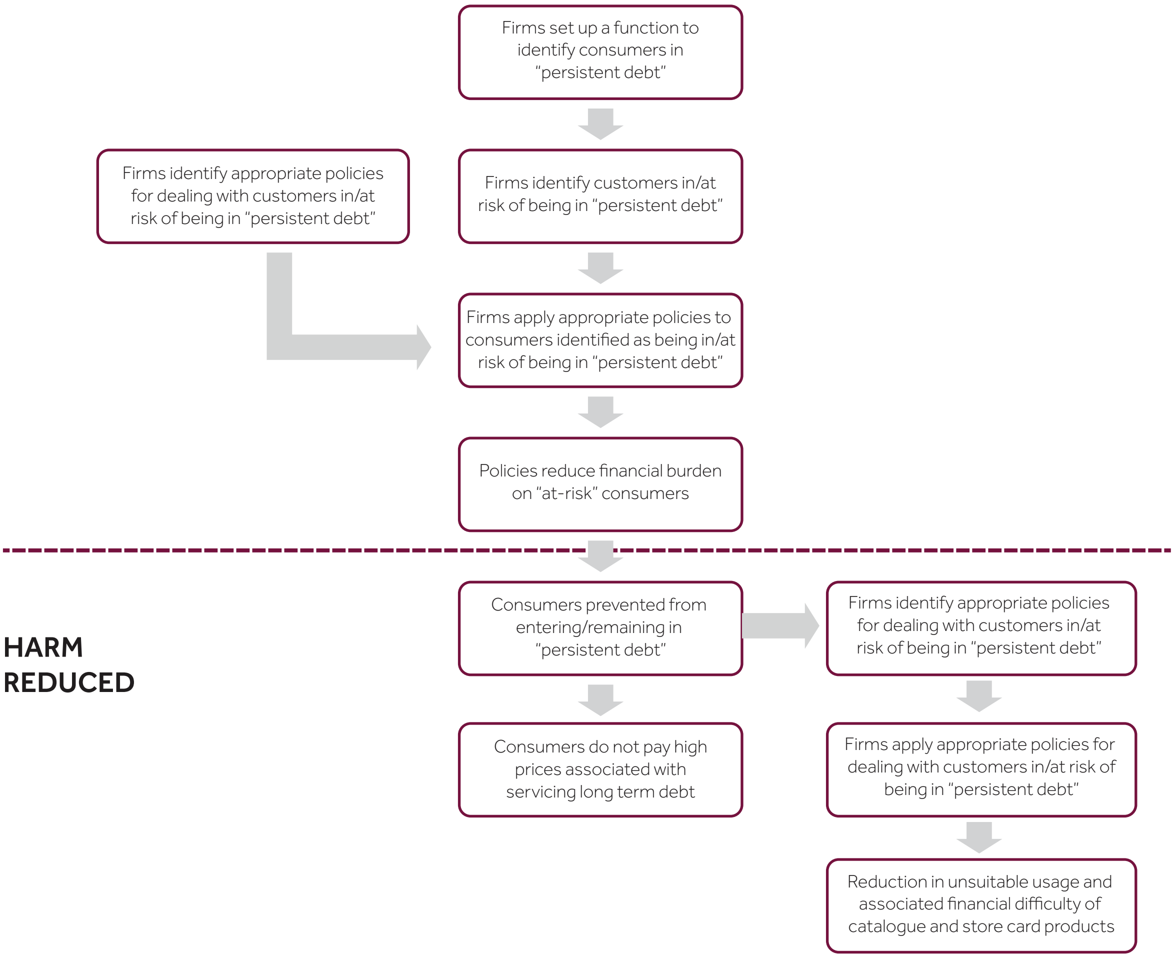
Intervention 4: Persistent Debt

Overview

302. This remedy is intended to address the harm to customers arising from the inappropriate use of catalogue and store card credit ie the use of such products for long term borrowing. Persistent debt arising from such activity is harmful as it is both indicative of an unsuitable product choice for servicing longer term borrowing, as well as a potential sign that customers are trapped in a debt spiral which they are unable to pay off.

100 Analysis of CRA data

Figure 5: Persistent Debt Proposals Causal Chain



Source: FCA Analysis

303. Our proposed remedy would encourage both firms and customers to avoid store card or catalogue debt becoming persistent, and for help customers who cannot afford to repay more quickly.

304. Persistent debt is defined as debt where over a period of 18 months, a customer pays more in interest, fees and charges than they have repaid of the principal. The rules do not apply to accounts where the balance has been below £200 in the previous 18 months.

Proposed Remedy

305. The proposed remedy requires firms to both identify and take appropriate action for consumers entering/ who are in persistent debt. This would take the following form, largely consistent with the rules on persistent debt for credit cards:

- At 18 months firms would need to prompt customers in persistent debt to change their repayment behaviour if they can afford to. Firms must tell customers about the potential implications of continuing with low repayments. The customer would also get the contact details of debt advice. Firms would need to assess whether customers are in persistent debt at least once a month.

- At 27-28 months firms would send a further reminder if payments indicate a customer is still likely to be in persistent debt at the 36 month point.

- At 36 months firms would need to intervene further if a customer remained in persistent debt. Firms would need to help the customer by proposing ways of repaying more quickly over a reasonable period, usually between 3 and 4 years. Where the customer is unable to repay more quickly, the firm must show forbearance (for example, by reducing, waiving or cancelling any interest or charges). We would expect firms to suspend the accounts of customers that have been shown forbearance, and those who do not respond.

Costs

306. We expect firms to incur compliance costs from these proposals.

307. Firms will incur costs from implementing a system to identify customers entering or already in persistent debt. This will include system costs involved in adapting pre-existing systems to identify individuals which fall under the definition of "persistent debt" as well as the costs of actually administering the firm's choice of intervention to those individuals may arise.

308. As for the previous interventions, we merely sum the responses of respondents to our survey of firms to create sector estimates of costs.

Table 12: One-off costs of setting up and running a function to identify customers that are in persistent debt and intervene to help them for Catalogue Credit and Store Card firms

	Cost Range per firm (£, 000)	Total Sector Cost (£, 000)
Catalogue	0 – 500	900
Store Card	100 – 300	400
Total	0 – 500	1,300

Source: FCA Analysis of Firm Survey Responses

Table 13: Ongoing costs (per annum) of setting up and running a function to identify customers that are in persistent debt and intervene to help them for Catalogue Credit and Store Card firms

	Cost Range per firm (£, 000)	Total Sector Cost (£, 000)
Catalogue	0 – 400	700
Store Card	100 – 600	800
Total	0 – 600	1,500

Source: FCA Analysis of Firm Survey Responses

309. The one-off costs of this remedy are approximately £900,000 for catalogue credit firms. For store card firms, this figure is £400,000. Reported ongoing costs are £700,000 for catalogue credit and £800,000 for the store card sector.

Benefits

310. We estimate three types of benefits from these proposals. Consumers who are in persistent debt for 18 months can benefit from the persistent debt proposals in one of the following ways:

- Avoiding being in persistent debt at 36 months by paying down their debt and making interest savings.

- Setting up a repayment schedule at 36 months that repays their debt more quickly and therefore saving on interest payments

- Consumers who cannot afford higher repayments after 36 months of persistent debt will be given forbearance and therefore benefit from lower interest payments.

311. We have not collected data similar to that collected for the Credit Card Market Study and following consultations, and we do not think it is proportionate to do so here. From the market study we have a much better understanding how consumers behave when using running account credit. We believe these lessons inform our approach. Further, the CCMS collected significant amounts of data which was used to estimate the costs and benefits of persistent debt remedies in that sector. We do not believe it is proportionate to burden firms with a large information request of the scale carried out for the market study to collect additional information for this sector for the purposes of this CBA. Given we have not collected account-level data; we have had to use additional assumptions in our estimation of benefits. We have used ranges rather than precise figures in some of our assumptions to reflect the uncertainty in the estimates. We have used a variety of data sources to develop our estimates of the benefits to consumers.

312. The use of ranges in the absence of precise figures helps to provide a reasonable benchmark estimate of the potential benefits to consumers, whilst acknowledging our lack of certainty. Even the use of account level data, would still result in considerable uncertainty about how consumers might react to the proposals and therefore the benefits that would be brought about by the remedies. We believe that our estimates encompass the likely range of outcomes, and therefore provide a useful illustration of potential benefits, given the inherent uncertainty we face.

313. We need to estimate the benefits for (i) the existing stock and (ii) new customers entering persistent debt.

314. To estimate the existing stock of customers in persistent debt, in our survey of firms, we asked firms about the number of consumers in persistent debt as defined as a customer paying more in interest and charges than they have repaid of the principal, over an 18 month period and a 36 month period, at 1 November 2017. Using this data, we estimate that for Catalogue credit the number of accounts in persistent debt is around 330,000 at the 18 month mark. The number of accounts in persistent debt at 36 months is 180,000.

315. For store card credit firms, the reported number of accounts in persistent debt is 290,000 at the 18 month mark and 180,000 at the 36 month mark.

316. We also need to estimate the number of new consumers entering persistent debt to estimate the benefits of the proposals for these consumers.

317. To estimate the number of consumers entering persistent debt each year we assume the number of consumers in persistent debt at the 36 month would stay fairly constant absent our proposals. We also need to estimate the average length of time a consumer would stay in persistent debt. If a consumer pays minimum repayments on their catalogue credit and continues to do so until the debt is paid off then on average they would stay in debt for 6.6 years. If they pay 20% above the minimum payment,[101] then they would repay their debt in 4.5 years. In contrast, for store cards, the time to repayment is 12 and 23 years respectively. This difference in repayment time is primarily driven by differences in minimum repayment rates; the weighted average rate is 2.5% for store cards, compared to 4.6% for catalogue firms.

Table 14: Numbers of consumers in persistent debt

	Catalogue	Store Cards
Current stock of consumers in persistent debt		
Consumers in persistent debt (18 months)	333,000	288,000
Consumers in persistent debt (36 months)	178,000	180,000
Consumers entering persistent debt each year		
Consumers in persistent debt (18 months)	90,000	58,000
Consumers in persistent debt (36 months)	16,000 – 23,000	5,000 – 9,000

Source: FCA Analysis of firm responses to our survey

318. To estimate the impact of the proposals on these consumers we assess the impact for three groups of consumers affected by our proposals:

- Group 1: Consumers who are likely to respond to communications at 18 months and so exit persistent debt before the assessment at 36 months.
- Group 2: Consumers who remain in persistent debt at 36 months and who are likely to agree a repayment schedule sufficient to repay the current balance within a reasonable period.
- Group 3: Consumers who remain in persistent debt at 36 months and are likely to have affordability difficulties and thus require forbearance in order to repay their balance within a reasonable period.

319. For the first group of consumers, we assume that in response to the communication at 18 months consumers increase their payments enough to avoid being in persistent debt at 36 months.

320. The second group of consumers agree to a repayment schedule to repay the outstanding balance over a set period of time. We assume that catalogue credit consumers pay down the debt over a 2 year period. This is reasonable because if the period was more than 2 years the initial payment would be lower than the minimum payment in that first month. For store cards, the repayment schedule is longer to avoid a large increase in payments for consumers. We assume a 4-year repayment schedule.

321. Finally, for store card customers the last group is unable to meet the repayment schedule so requires some forbearance. We again assume that consumers pay off their debt in 24 months for catalogue credit but 48 months for store cards. However, we assume that consumers are unable to afford the repayments on such a schedule and forbearance is given for these consumers. We assume that a 25% reduction in interest is applied to the account. If we had a higher reduction in the interest rate,

101 This creates a range for savings a consumer would make from the interventions. We note that payments cannot be much in excess of this level as it would mean the consumer pays more in repayments than interest. This would mean the persistent debt definition does not apply to the consumer.

consumers would be required to pay less than the minimum payments they are already making on the debt.

322. In all three scenarios, and under the counterfactual, we assume that consumers do not make any additional purchases following 18 months in persistent debt as a result of paying down balances under our proposals. The benefits to consumers would be reduced if lower balances from our proposals lead to increased spending and therefore additional interest on this spending. We think this is plausible given that consumers have been discouraged by the proposals from additional spending and additional spending is much less likely than on credit cards where there is a much wider choice of spending.

323. From the survey of firms, we calculate a weighted (by number of accounts in persistent debt) average initial balance at 18 months.

Table 15: Account characteristics for those in persistent debt

	Catalogue	Store Cards
Weighted Average balance at 18 months, £	£849	£841
APR, %	41.9%	27.3%
Contractual minimum repayment, %	4.6%	2.5%
Contractual minimum repayment, £	£6.28	£4.99

324. We assume that under each group consumers have the same average balances.[102] We might expect that those consumers better able to pay their debts might have different account balances. We therefore do not think this assumption will materially bias our results.

325. We also make a number of other assumptions to enable us to generate our estimates.

- We assume that between 0-30% of consumers do not engage with any of the communications or they default after spending 36 months in persistent debt. We do not account for any benefits for these consumers.

- We assume that all consumers pay the minimum repayment or 20% above the minimum payment until the debt is repaid. This is a reasonable assumption given that if the repayments are too high consumers no longer meet the persistent debt criteria.

- In line with the credit cards CBA, we apply the following assumptions to the existing stock of consumers. We assume that of the consumers that respond to the communications, 11% are in a position such that a relatively small increase in repayments would lead the account to exit persistent debt before 36 months, 63% would agree to a repayment schedule and 26% are accounts with affordability difficulties

- For the new flow of consumers hitting the 18-month PD threshold, we again use assumptions in line with the credit cards CBA. We assume that 16% could exit persistent debt with a relatively small increase in repayment and so are expected to exit persistent debt before 36 months based on the data we received on customer response rates. 52% are in a position to agree to an affordable repayment schedule

102 We note average balances for consumers in persistent debt on a credit card was £3,624. See FCA CP17/10, page 75.

and 32% are in a position such that only a repayment schedule with interest rate forbearance is affordable.

- We acknowledge that many of these consumers will be being offered forbearance in absence of the proposed remedy. We assume that 20-40% of these consumers meeting the persistent debt criteria will be receiving forbearance and hence not pay interest. Consequently, no interest savings will accrue to these consumers as a result of the persistent debt remedies. We use this range as around 30% of catalogue credit accounts eventually default.[103, 104]

326. The credit card CBA assumptions provide us with a useful benchmark to evaluate the characteristics of consumers responding to communications. We note that while these proportions may vary in the store card and catalogue credit market when compared to the credit card market. We do not believe that varying these proportions will materially change our estimates, and are thus useful in providing an illustration of potential benefits.

327. The key assumption we use from credit cards is the proportions of consumers that respond to the communication at 18 months (11% and 16% for the stock and flow respectively). We expect a modest proportion of consumers will change their repayment behaviour following the notification they receive at 18 months. Generally, we expect some consumers to actively respond to communications but only a relatively small proportion to do so. If the proportion was lower, more consumers would receive the higher benefits available from the using repayment schedules to pay off their debt, and our benefits would be higher overall. If the proportion was higher, this would reduce the overall benefits but we do not think it is plausible that significant numbers of consumers will actively alter their repayment behaviour consistently over the following 18 months.

328. We might expect higher numbers of consumers to increase payments as a result of the 18 month communication, than for credit cards, as the repayments required are relatively low (due to low average balances). However, consumers are likely to be below median wage and even small increases in repayments may pose difficulties for consumers. We know these consumers may suffer from present and optimism bias and therefore even if consumers intend to increase their repayments, we might expect that many consumers do not stick to these overpayments. Therefore given the uncertainty around the proportion, we consider the proportion used is reasonable.

329. The impact of the other proportions makes less difference to the overall interest savings to consumers. Diverting consumers from a repayment schedule without forbearance to one with forbearance makes much less difference to the overall benefits, due to the similar levels of interest savings.

330. We use different assumptions for the stock of consumers in persistent debt and the consumers who enter into persistent debt each year. This is because we would expect new consumers entering persistent debt are likely to have different characteristics to those consumers who have been in persistent debt for potentially a significant amount of time.

103 See technical annex
104 The proportion is lower for store cards so we may overstate the number receiving forbearance and therefore understate the benefits.

331. Many of the interest savings are many years into the future. To take account of this, we have converted the savings into current prices (taking account of inflation.)[105] We have also discounted the saving at 3.5% per annum to take into account[106] the general preference for consumption today rather than in the future. This allows us to sum different benefits at different points in time.

332. For the existing stock of consumers in persistent debt, we estimate the following interest rate saving from the proposals for catalogue credit. Table 16 shows the interest savings for those currently in persistent debt (the current stock in persistent debt).

Table 16: Total and average savings until the balance is cleared for existing stock of Catalogue consumers in persistent debt

	All consumers in persistent debt at 36 months	Consumers that exit Persistent Debt before 36 months	Consumers on repayment schedule	Consumers with affordability difficulties
Number of consumers	178,000	11,000 – 12,000	63,000 – 67,000	26,000 – 28,000
Total savings, £m	19 – 46	0 – 4	13 – 29	6 – 13
Average saving, £	110 – 260	20 – 310	200 – 430	240 – 490

Source: FCA Analysis
Note: Due to rounding total figures may not add up

333. Table 17 shows the interest savings for consumers that enter persistent debt each year.

Table 17: Total and average savings until the balance is cleared for new yearly flow of Catalogue consumers in persistent debt, ongoing per year

	All consumers in persistent debt at 36 months	Consumers that exit Persistent Debt before 36 months	Consumers on repayment schedule	Consumers with affordability difficulties
Number of accounts	16,000 – 23,000	2,000 – 2,000	5,000 – 6,500	4,000 – 4,000
Total savings, £m	1.8 – 5.4	0.0 – 0.6	1.0 – 2.8	0.8 – 2.0
Average saving, £	80 – 350	20 – 310	200 – 430	240 – 490

Source: FCA Analysis
Note: Due to rounding total figures may not add up

334. For the existing stock of consumer in persistent debt, we estimate the following interest rate saving from the proposals[107] for Store Card credit. Table 18 and Table 19 set out the interest savings for consumers in persistent debt on Store Cards. Table

105 We assume the inflation will be 2%, the target for the inflation rate set by Government.
106 HM Treasury, The Green Book: Central Government Guidance On Appraisal And Evaluation, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/685903/The_Green_Book.pdf, see Annex 6.
107 Some firms reported that they had included consumers that are receiving forbearance in the figures reported on those in persistent debt. This will mean our estimates of the number of consumers will be an over- estimate as will our estimates on the benefits to consumers.

18 shows the interest savings for those currently in persistent debt (the current stock in persistent debt). Table 19 shows the interest savings for consumers that enter persistent debt each year.

Table 18: Total and average savings until the balance is cleared for existing stock of Store Card consumers in persistent debt

	All consumers in persistent debt at 36 months	Consumers that exit Persistent Debt before 36 months	Consumers on repayment schedule	Consumers with affordability difficulties
Number of accounts	180,000	11,000 – 12,000	64,000 – 68,000	26,000 – 28,000
Total savings, £m	48 – 113	2 – 9	31 – 71	15 – 32
Average saving, £	260 – 620	180 – 780	480 – 1,050	570 – 1,140

Source: FCA Analysis
Note: Due to rounding total figures may not add up

335. Table 19 shows the saving in interest payments for the consumers entering persistent debt each year.

Table 19: Total and average savings until the balance is cleared for new yearly flow of Store card consumers in persistent debt, ongoing per year

	All consumers in persistent debt at 36 months	Consumers that exit Persistent Debt before 36 months	Consumers on repayment schedule	Consumers with affordability difficulties
Number of accounts	5,000 – 9,000	1,000 – 1,000	1,800 – 1,900	1,100 – 1,200
Total savings, £m	1.7 – 3.6	0.1 – 0.4	0.9 – 1.9	0.7 – 1.3
Average saving, £	190 – 830	180 – 780	480 – 1,050	570 – 1,140

Source: FCA Analysis
Note: Due to rounding total figures may not add up

336. Over time, we would expect to see fewer consumers in persistent debt. This change will arise from changes in both consumer and firm behaviour.

337. We also note that the benefits to consumers in most instances are transfers from firms. Lower interest payments also results in lower revenue for firms.

Other benefits

338. We note that more sustainable borrowing and debt is likely to deliver other benefits for consumers and firms.

339. Firms will use fewer resources in collecting missed payments. They will also have lower financing costs and lower administration costs on accounts once an account is paid off.

340. Consumers will avoid some of the costs of problem debts, such as stress, contingent fees, and the cost of forgoing necessary consumption (such as food and heating).

We might also expect that in response to our proposals some firms might increase minimum repayments to consumers to avoid persistent debt problems. This will mean that consumers may be better able to assess the true price of the product and be less likely to make purchases where the price of the product exceeds the value that the consumer places on it.

341. In addition to interest savings by consumers, the reduction in balances which may be prompted by the remedy may increase the flexibility of certain customers in responding to unexpected income shocks. This increase in flexibility will arise from the increased availability of credit resulting from paying down their balance. This will likely reduce the stress associated with such income shocks.

Conclusion

342. Overall we expect our remedies to be net beneficial to the sector. The compliance costs are relative small, at £1.3m one-off and £1.5m ongoing, compared to the interest saving that consumers would receive from the proposals. We estimate the interest savings to consumers to be in excess of £68m during the first 10 years of our proposals. We note the wide range of potential benefits that will be brought about for consumers. While the size of the benefits to consumers is uncertain, the lower bound of the range of benefits we have estimated for consumers substantially outweighs the costs. While a significant proportion of these costs are transfers to consumers from firms, there are likely to significant benefits from ensuring consumers do not sit on balances for significant periods paying huge amounts of interest relative to the amount borrowed.

Annex 3
Compatibility statement

Compliance with legal requirements

1. This Annex records the FCA's compliance with a number of legal requirements applicable to the proposals in this consultation, including an explanation of the FCA's reasons for concluding that our proposals in this consultation are compatible with certain requirements under the Financial Services and Markets Act 2000 (FSMA).

2. When consulting on new rules, the FCA is required by sections 138I(2)(d) FSMA to include an explanation of why it believes making the proposed rules is:

   a. compatible with its general duty, under s. 1B(1) FSMA, so far as reasonably possible, to act in a way which is compatible with its strategic objective and advances one or more of its operational objectives, and

   b. its general duty under s. 1B(5)(a) FSMA to have regard to the regulatory principles in s. 3B FSMA. The FCA is also required by s. 138K(2) FSMA to state its opinion on whether the proposed rules will have a significantly different impact on mutual societies as opposed to other authorised persons.

3. This Annex also sets out the FCA's view of how the proposed rules are compatible with the duty on the FCA to discharge its general functions (which include rule-making) in a way which promotes effective competition in the interests of consumers (s. 1B(4)). This duty applies in so far as promoting competition is compatible with advancing the FCA's consumer protection and/or integrity objectives.

4. This Annex explains how the FCA has had regard to the recommendations made by the Treasury under s.1JA FSMA about aspects of the economic policy of Her Majesty's Government to which the FCA should have regard in connection with its general duties.

5. This Annex refers to our assessment of the equality and diversity implications of these proposals.

6. Under the Legislative and Regulatory Reform Act 2006 (LRRA) the FCA is subject to requirements to have regard to a number of high-level 'Principles' in the exercise of some of our regulatory functions and to have regard to a 'Regulators' Code' when determining general policies and principles and giving general guidance (but not when exercising other legislative functions like making rules). This Annex sets out how we have complied with requirements under the LRRA.

The FCA's objectives and regulatory principles: Compatibility statement

7. The proposals set out in this consultation are primarily intended to advance the FCA's operational objective of achieving an appropriate degree of protection for consumers. They are designed to protect consumers from harm we have identified from using high-cost credit products during the course of the high-cost credit review.

Rent-to-own

8. Our proposal to ban the sale of extended warranties as an add-on alongside the hire purchase agreement is intended to address the information asymmetry and point of sale advantage held by RTO firms in selling extended warranties. This is to address the risk of consumers paying for expensive warranties in addition to the wider costs of using RTO services where they are not clear whether this is mandatory or what benefits the product provides. We consider that our proposals will allow consumers to make significant savings on extended warranty products they may not feel they need, either by not purchasing the warranties and claiming on manufacturers' warranties if necessary, or potentially by purchasing from elsewhere. This is important given the low incomes of many consumers using RTO and in the context of the wider costs paid by consumers in using RTO. Those that do wish to purchase extended warranties are able to make a considered decision on this.

9. In considering this proposal we have had regard to the matters set out in s.1C(2)(a)-(h) FSMA:

- *s.1C(2)(a) differing degrees of legal risk involved in different kinds of investment:* we do not consider that this is relevant to this proposal.
- *s.1C(2)(b) differing degrees of experience and expertise of consumers:* we believe this proposal helps consumers to be better informed to make a decision on whether they wish to purchase an extended warranty or not, by providing clearer information and a deferred opt-in.
- *s.1C(2)(c) timely provision of advice and information which is accurate and fit for purpose:* we consider that these measures will improve the information given to consumers at point of sale.
- *s.1C(2)(d) general principle that consumers take responsibility for their decision:* this proposal is intended to help consumers take better decisions regarding the purchase of extended warranties.
- *s1C(2)(e) general principle that providers provider appropriate level of care:* we believe that this measure will allow for consumers to be treated with the appropriate level of care in helping consumers to take better informed decisions on the purchase of extended warranties.
- *s1C(2)(f) differing expectations of consumers:* we do not consider that this is a relevant consideration.
- *s1C(2)(g) any MAS information provided to the FCA:* we have had regard to information provided to us by MAS throughout the course of the Review.
- *s1C(2)h) any FOS information provided to the FCA:* we have not received any information from FOS on the issues at hand which would have impacted our proposals.

10. We consider that all our proposals in relation to RTO are compatible with the FCA's strategic objective of ensuring that the relevant markets function well because they address market failures we see where potentially vulnerable consumers are sold products which may not be suitable for them. Our proposals will provide greater balance between consumers and firms in understanding extended warranties and ensure consumers are aware of the options available to them. Our proposals are not seeking to restrict the availability of add-on services but help consumers make their own assessment of the suitability of financial products for them, which we think will result in better outcomes for consumers. We have undertaken a full CBA which has found that consumers will benefit from our proposals, and we believe that the measures we are proposing are proportionate to the harm.

Home-Collected Credit

11. Our proposals on home-collected credit are intended to address the risks of harm to consumers from repeat borrowing.

New Rules

12. Our first proposal requires firms to give information on the comparative costs of borrowing when consumers want to take out new loans. Refinancing (using part of a new loan to pay off an old one) is commonplace in the sector. Our evidence suggests this is partly driven by consumers but may also be prioritized by firms over the issue of an additional concurrent loan. Refinancing tends to result in weekly repayments being kept low (a priority for many consumers on stretched budgets) but can be more costly overall. We think this proposal will benefit all consumers by setting out in simple terms the difference in costs in both total cost of credit and weekly repayment terms so they are better able to choose the arrangement they feel is most suitable for them.

13. In considering this proposal we have had regard to the matters listed in s1C(2)(a)-(h) of FSMA:

- *s.1C(2)(a) differing degrees of legal risk involved in different kinds of investment:* we do not consider that this is relevant to this proposal.

- *s.1C(2)(b) differing degrees of experience and expertise of consumers:* we believe this proposal helps consumers to be better informed to make a decision on how they wish to take on additional borrowing but protecting those that are potentially vulnerable from undue sales influence and making options to consumers clearer.

- *s.1C(2)(c) timely provision of advice and information which is accurate and fit for purpose:* we consider that these measures will improve the information given to consumers at the time at which they inform a firm that they wish to borrow more.

- *s.1C(2)(d) general principle that consumers take responsibility for their decision:* this proposal is intended to help consumers take better decisions regarding additional borrowing.

- *s1C(2)(e) general principle that providers provide appropriate level of care:* we believe that this measure will allow for consumers to be treated with the appropriate level of care in helping consumers to take better informed decisions on additional borrowing.

- *s1C(2)(f) differing expectations of consumers:* we do not consider that this is a relevant consideration.

- *s1C(2)(g) any MAS information provided to the FCA:* we have had regard to information provided to us by MAS throughout the course of the Review.
- *s1C(2)h) any FOS information provided to the FCA:* we have not received any information from FOS on the issues at hand which would have impacted our proposals.

New Guidance

14. We are concerned that some consumers may be using home-collected credit on a longer term basis as a result of firms being able to unduly influence consumers to take out further loans, in the course of their regular collections. While there are some safeguards in place in both our rules and firms' policies around repeat borrowing we are consulting on new guidance on the s.49 Consumer Credit Act 1974 prohibition on canvassing and soliciting borrower-lender agreements off-trade premises, which clarifies that discussions on further lending are always started by consumers and not representatives working for the home-collected credit firms. Repeat borrowing is important to this consumer base, enabling access to credit in order to manage unexpected expenditure. However, we consider it is necessary to consult on this guidance in order to protect consumers from being influenced to take out more loans. Firm representatives are generally incentivised to maximise collections and the nature of the in-home collection and personal relationship between the consumer and firm representative may also enable firms to take the lead in repeat borrowing. The guidance will mitigate the effects of this.

15. We consider that all our proposals concerning home-collected credit are compatible with the FCA's strategic objective of ensuring that the relevant markets function well because they address market failures we see in high-cost credit where potentially vulnerable consumers are sold products which may not be suitable for them. Our proposals will provide greater balance between consumers and firms in understanding of products and ensure consumers are aware of the options available to them. Our proposals are not seeking to restrict the availability of forms of credit but help consumers make their own assessment of the suitability of financial products for them, which we think will result in better outcomes for consumers. We have undertaken a full CBA which has found that consumers will benefit from our proposals, and we believe that the measures we are proposing are proportionate to the harm.

Catalogue credit and store cards

16. Our proposals on catalogue credit and store cards are intended to advance the FCA's operational objective of achieving an appropriate degree of protection for consumers by addressing potential harm arising throughout the customer journey.

17. The intention of our proposals in relation to Buy Now Pay Later (BNPL) or similar deals, are to require catalogue credit and store card firms to be clearer about the consequences of not repaying within the offer period, in particular that a lump sum of interest will be added to their account. Our proposals on a clear, prominent, timely notice to the customer before the end of a BNPL or similar offer ends is similarly intended to provide customers with clarity to enable them to make informed decisions on repayment within this period.

18. We intend that our proposals to provide greater control and choice to catalogue customers, consistent with those protections for credit cards and store cards would provide protection to customers who might spend more than they would otherwise intend to.

19. Our proposals requiring earlier intervention by catalogue credit firms to identify those at risk of potential financial difficulties are intended to prompt firms to take action before these difficulties develop. They would require firms to use the data that they have available to identify these customers and take appropriate steps.

20. Our proposals with regard to persistent debt are to address the market failure where a number of catalogue credit and store card customers carry a large balance for a long time without significantly reducing their debt. This is a consequence of the feature for both products which allows customers to how much to repay as long as they meet the minimum repayment. This has financial implications for customers in the form of high debt servicing costs and we consider that there are no incentives for firms to intervene earlier where customers do not fall into arrears and continue making payments. The proposed remedies seek to align the incentives for firms and customers by encouraging earlier repayment where this is possible or to provide forbearance to those customers who struggle to repay.

21. In considering these proposals we have had regard to the matters listed in s.1C(2)(a)-(h) of FSMA – in particular, matters in s.1C(2)(b)-(d) of FSMA.

22. Section 1C(2)(a) differing degrees of legal risk involved in different kinds of investment: we do not consider that this is relevant to these proposals.

23. Section 1C(2)(b) differing degrees of experience and expertise of consumers: we consider that the remedies will reflect the differing degrees of experience and expertise that different consumers may have in the following ways.

- **a.** Our proposals on BNPL will be of particular benefit in helping to ensure that customers are better informed about the consequences of taking up a BNPL offer. The proposal to receive clear, timely notification when this offer period will end will also assist catalogue credit and store card customers make decisions on whether to take products under this offer and on their repayment decisions.

- **b.** We expect that our proposals to provide greater choice and control to catalogue credit customers will provide greater protection to customers who might otherwise be at risk of spending more, absent this choice and control.

- **c.** Our proposals to require catalogue credit and store card firms to identify, contact and take appropriate action where customers at risk of financial difficulties will particular enhance protection of sub-prime and vulnerable customers.

- **d.** Our proposals on persistent debt take into account the different degrees of experience and expertise that customers will have and ensure that customers receive appropriate interventions according to their ability to repay. Accordingly, some customers who can repay quicker will be expected to amend their repayment behaviour whereas those who cannot will be treated with forbearance and due consideration.

24. Section 1C(2)(c) timely provision of advice and information which is accurate and fit for purpose: we consider that these measures will reflect the needs that consumers may have as follows.

- **a.** Our proposals on BNPL offers will ensure that catalogue credit and store card firms provide an adequate explanation as well as a clear, timely prompt prior to the ending of an offer. We consider that these requirements will enhance the ability of customers to take well-informed decisions on buy now pay later based on clear, timely information.

b. Our proposals to provide greater choice and control to catalogue credit customers on credit limit will require firms to provide notice of a proposed increase at least 30 days before the increase comes into effect (with exceptions) and enable customers to opt out of receiving credit limit increases or offers of these.

c. Our proposals on earlier intervention will require catalogue credit and store card firms to take appropriate action where a customer is identified as at risk of financial difficulties. Such action could include providing information to customers on the risks of escalating debt as well as additional interest or charges. We consider that this requirement will ensure consistency in the information that customers receive across the catalogue credit and store card markets.

d. Our proposals on persistent debt explicitly recognise the importance of timely accurate information and advice that is fit for purpose. For example, firms would be required to inform customers at the 18 month point on the need to repay more quickly and the implications of failing to do so in terms of costs and the risk of further interventions in the subsequent 18 months. Firms would also be required to remind customers at the midway point in the subsequent 18 months on the need to repay more quickly.

25. Section 1C(2)(d) general principle that consumers take responsibility for their decision: we consider that the remedies will reflect this principle as follows.

a. Our proposals on BNPL offers will ensure that catalogue credit and store card customers are provided with clear, timely information that is sufficient to allow them to make decisions on whether to take out these offers and make judgments on how to address risks including whether to change their repayment behaviour.

b. Our proposals to provide greater choice and control to catalogue credit customers on credit limit will enhance customer's decision making and responsibility on whether and in what circumstances to receive offers of credit limit increases.

c. Our proposals on earlier intervention are intended to place greater responsibility on catalogue credit and store card firms to intervene earlier and take appropriate steps where consumers are at risk of financial difficulties. In some circumstances, such action will result in consumers being invited to take the initiative – for example, where they are notified of escalating debt and so to modify their repayment behaviour.

d. Our proposals on persistent debt have been shaped by this principle. For example, the interventions prior to the period of 36 months require firms to invite customers to alter their repayment behaviour and repay more quickly, where they can afford to do so.

26. Section 1C(2)(e) general principle that providers provide appropriate level of care: we believe this measure will allow for consumers to be treated with the appropriate level of care in helping consumers to take better informed decisions on additional borrowing and repayment behaviour.

27. Section 1C(2)(f) differing expectations of consumers: we do not consider that this is a relevant consideration.

28. Section 1C(2)(g) any MAS information provided to the FCA: we have had regard to information provided to us by MAS throughout the course of the Review.

29. Section 1C(2)(h) any FOS information provided to the FCA: we have considered information from FOS and have not received any information that would impact on our proposals.

30. The following paragraphs apply to all the proposals in our publication.

31. In preparing the proposals set out in this consultation, the FCA has had regard to the regulatory principles set out in s. 3B FSMA.

The need to use our resources in the most efficient and economic way

32. We consider that the proposals are compatible with this principle, on the basis that we have identified specific harms to consumers from using high-cost credit products; so we consider that using FCA resources to design and consult on remedies which address these harms is proportionate.

The principle that a burden or restriction should be proportionate to the benefits

33. We have given careful consideration to the proportionality of proposed interventions. Where there are additional burdens on firms we have assessed that these are outweighed by benefits for consumers; ie the potential financial benefit of being able to make better informed decisions (eg on repeat borrowing in home-collected credit, or whether to buy extended warranties on goods taken out on hire-purchase). We have similarly considered this principle in respect of credit limit increases and buy now pay later offers for catalogue credit firms for the former and catalogue credit and store card firms for the latter. We have collected data from firms on the costs of these additional restrictions in order to inform this assessment, and we think that these measures may help align incentives for customers and firms. We have drafted our proposed rules in a manner which provides firms with some flexibility where appropriate (eg on the exact form of disclosure to be given on the features of extended warranties) and reflects diversity of firm's business models.

The desirability of sustainable growth in the economy of the United Kingdom in the medium or long term

34. We have had regard to this principle in developing our proposals. Given the size of the markets in question we do not think that our proposals will have a negative impact on sustainable growth in the UK economy in the medium or long term.

The general principle that consumers should take responsibility for their decisions

35. Our proposals for home-collected credit and RTO products are intended to ensure consumers are able to make better decisions and ultimately take responsibility for their decisions. We see significant information asymmetries between consumers and firms which act against the interests of consumers being able to take measured decisions at present, and our proposals seek to address these.

The responsibilities of senior management

36. We do not consider that this principle is relevant to our proposals as we do not create or affect any responsibilities directly placed on senior management.

The desirability of publishing information relating to persons subject to requirements imposed under FSMA, or requiring them to publish information

37. This principle is not relevant to our proposals as they do not involve any requirements imposed under the FSMA, nor do we require them to publish additional information.

The principle that we should exercise of our functions as transparently as possible

38. In the development of our proposals we have had regard to the importance of acting as transparently as possible. We have gathered evidence on the markets we are examining under the high-cost credit review since November 2016 when we published our Call for Input. We have since published a Feedback Statement and update document setting out our provisional analysis of harm, and have gathered evidence from firms on the costs of our proposed remedies prior to publication.

39. In formulating these proposals, the FCA has had regard to the importance of taking action intended to minimise the extent to which it is possible for a business carried on (i) by an authorised person or a recognised investment exchange; or (ii) in contravention of the general prohibition, to be used for a purpose connected with financial crime (as required by s. 1B(5)(b) FSMA).

Expected effect on mutual societies

40. The FCA does not expect the proposals for rules and guidance in this paper to have a significantly different impact on mutual societies. We are not aware of any mutual societies providing the type of credit which our proposed measures concern. There may be indirect effects arising from our proposals to encourage more referrals to credit unions by social landlords. In turn, this may reduce the number of people turning to high-cost credit including rent-to-own, home-collected credit and catalogue credit.

Equality and diversity

41. We are required under the Equality Act 2010 to have 'due regard' to the need to eliminate discrimination, foster good relations and to promote equality of opportunity in carrying out our policies, services and functions. As part of this, we conduct an equality impact assessment to ensure that the equality and diversity implications of any new proposals considered.

42. The outcome of this assessment in this case is at Annex 4.

Compatibility with the duty to promote effective competition in the interests of consumers

43. In preparing the proposals as set out in this consultation, we have had regard to the FCA's duty to promote effective competition in the interests of consumers (s1B(4) FSMA). Our proposals are primarily intended to fulfil our consumer protection objective. However there may be some positive impacts on competition resulting from our proposals which work in the interests of consumers, in line with s1B(4) FSMA. Taking account of the factors in s1E(2) FSMA we have had regard to:

a. *The needs of different consumers who use or may use those services, including their need for information that enables them to make informed choices:* our proposals are intended to provide clearer information to consumers to help them make informed choices, for example on whether to purchase extended warranties or refinance home-collected credit loans or for catalogue and store card consumers on whether to take out a buy now pay later offer

b. *The ease with which consumers who may wish to use those services, including consumers in areas affected by social or economic deprivation, can access them:* Many of the consumers in question are in areas affected by social or economic deprivation, and our proposals are not intended to restrict access to services but to help consumers make informed decisions on whether they wish to use them or not, and how they use them.

c. *The ease with which consumers who obtain those services can change the person from whom they obtain them* we are of the view that although the primary intention of our proposals is to protect consumers there may be some pro-competition effects such as switching. For example our proposals on the sale of extended warranties by RTO firms may encourage consumers to shop around and purchase these elsewhere, which could in turn help stimulate competition on prices. In addition our measures to improve information provision and reduce undue sales influence over existing customers in home-collected credit may result in consumers deciding to consider approaching other lenders. This follows the Competition Commission's study into home-collected credit which sought to boost competition in this market.

d. *The ease with which new entrants can enter the market:* we do not consider that any of our proposals will prevent any new entrants from entering the market

e. *How far competition is encouraging innovation:* we do not consider that any of our proposals will encourage or suppress innovation.

Recommendations made by the Treasury under s. 1JA FSMA about aspects of the economic policy of Her Majesty's Government to which we should have regard in connection with our general duties.

44. We have had regard to the recommendations made by the Treasury under s.1JA FSMA about aspects of the economic policy of Her Majesty's Government to which we should have regard in connection with our general duties.

45. We consider that our proposals are consistent with the government's policy to achieve strong, sustainable and balanced growth. We note that price and financial stability are essential pre-requisites for strong, sustainable and balanced growth in all regions and sectors of the UK economy. We have had regard to competition, growth, competitiveness, innovation, trade and better outcomes for consumers in designing these proposals.

46. In addition the Chancellor noted in his letter dated 8 March 2017 his support for the FCA's commitment to "look in more detail at high cost credit, including overdrafts, from a consumer protection as well as a competition perspective, using its full range of powers".

Annex 4
Equality and Diversity Assessment

1. We are required under the Equality Act 2010 in exercising our functions to 'have due regard' to the need to eliminate discrimination, harassment, victimisation and any other conduct prohibited by or under the Act, advance equality of opportunity between persons who share a relevant protected characteristic and those who do not, and foster good relations between people who share a protected characteristic and those who do not. Protected characteristics include age, gender, disability, race or ethnicity, pregnancy and maternity, religion, sexual orientation and gender reassignment.

2. As part of this, we ensure the equality and diversity implications of any new policy proposals are considered. This annex sets out the results of our initial assessment, explaining the potential impact of our proposals on protected groups where we have identified them and where relevant the steps we have taken or will take to minimise them.

Summary

3. In summary our initial assessment has found that our proposals do not result in direct discrimination for any groups with protected characteristics. We have identified that groups with protected characteristics (eg gender and disability) make up the majority of home-collected credit and rent-to-own consumers; however we anticipate our proposals will have a net positive impact on consumers and those with the protected characteristics of gender and disability.

4. The equality impact assessment (EIA) process is ongoing and will not be completed until we develop and publish our final policy. As a result we are seeking additional input from all stakeholders to help us further investigate and establish the extent of any potential impacts of the proposals in this paper. We would also welcome any comments or information respondents may have on any equality and diversity issues they believe arise from these proposals.

5. We are consulting on a range of measures to address harms we have identified during the high-cost credit review. These are:

Rent-to-own (RTO)
Measures to protect consumers from harm from high prices:

- A "point of sale ban" on extended warranties to ensure consumers have adequate information and time to make a decision on whether to purchase high-cost insurance products.
- We also discuss potential further intervention on high pricing in the RTO sector, subject to further analysis, but we are not consulting on any measures at this stage.

Home-collected credit
Measures to protect consumers in the repeat borrowing process:

- New guidance on canvassing off trade premises to ensure repeat borrowing is driven by consumers and not firms, and;
- A new information remedy to ensure consumers are told the comparative costs of different types of repeat borrowing when they wish to borrow more.

Catalogue credit
Measures to protect consumers from a range of harms including:

- Extend existing rules for credit cards and store cards to give customers greater choice and control over credit limit increases
- Measures to prevent firms from increasing interest rates for those at risk of financial difficulties
- Rules requiring further information to be given to consumers on the potential costs of Buy Now Pay Later.
- Rules to require firms to intervene to identify consumers at risk of financial difficulty and take appropriate steps to address this.

Consumer Demographics

6. We have a range of data sources informing our understanding of consumers which use different forms of high-cost credit; some informed by our own work and other FCA sources, and some from firms, debt charities and other external sources:

Rent-to-own

7. We know that consumers that use RTO are at a high risk of financial vulnerability. Our analysis of a large representative sample of credit reference agency (CRA) data found that they have a median income of £16,100 and a median outstanding debt of £4,300.

8. Our consumer research found that many RTO consumers were from low income households, including people out of work (either due to sickness and/or claiming benefits, or single parent households. This has led us to consider that the impact of any proposals we make will have a disproportionate impact on groups with protected characteristics (gender, disability, pregnancy/maternity.).

9. Citizen's Advice's analysis of the Wealth and Assets Survey found that 45% of RTO consumers are in the bottom 20% of earners, 55% have dependent children, 77% are renting, and 43% are disabled or have a long term illness.[1]

10. The All Party Parliamentary Group enquiry into Household Debt found through information from firms that 50% of consumers using RTO are wholly or partly reliant on benefit income, usually aged 22-49, up to 78% are female, 60% have children, and 94% live in rented accommodation.[2]

Home-Collected Credit

11. Our evidence suggests this is a very similar demographic to RTO. Our CRA data analysis reveals a median income of £15,500, with a median outstanding debt of £2,800.

1 https://www.citizensadvice.org.uk/Global/CitizensAdvice/Debt%20and%20Money%20Publications/FINALRENTTOOWNREPORT%20(4).pdf
2 http://www.appgdebt.org/wp-content/uploads/2017/08/APPG-RTO-Inquiry-report-10-2-15web.pdf

12. The Financial Lives survey included a small sample of home-collected credit consumers (114). It suggested consumers in this market are predominantly female (67%), young (49% aged 25-44 compared with 34% of the whole population), had a lower education level (only 23% educated beyond GCSE level), many were unemployed (14%) and a much larger proportion were single with children (34%) than the population more broadly (9%). 77% of all home-credit users were renting and 55% reported having a physical or mental condition expected to last more than 12 months (24% in broader population).

13. Our consumer research confirmed home-collected credit and RTO users have a clear demographic overlap– (low income, high financial pressure, consumers off work sick and/or claiming benefits, single parent households). Again, we consider that any proposals will have a disproportionate impact on some groups with protected characteristics (sex, disability, pregnancy/maternity)

14. Citizen's Advice's analysis of the Wealth and Assets Survey shows that doorstep loan customers were more likely to experience vulnerability or live in an insecure situation. Half of the consumers are in the lowest earning fifth of adults, the majority (90%) are renting and nearly 40% have a long term illness or disability.[3]

Catalogue credit and store cards

15. Our evidence suggests that catalogue credit customers have slightly higher median annual income compared with rent-to-own and home-collected customers: £17,700 in 2016, with a median outstanding debt of £1,300.

16. The Financial Lives survey included a sample of catalogue credit consumers. It suggested consumers in this market are predominantly female (79%). They have a median average of 45 (with most falling into the 35-44 age group – 26%), the majority are employed (66%) with the next largest group being retired (12%), with 44% educated beyond GCSE level). A large number of catalogue credit customers were in rented accommodation (43%) and 25% reported having a physical or mental condition expected to last more than 12 months.

17. Store card customers have a similar median annual income to catalogue credit customers: £17,500, median outstanding debt of £1100.

18. The Financial Lives survey included a sample of store card consumers. It suggested a similar trend to catalogue credit with most consumers in this market being female (68%). They have a lower median age of 36. A smaller proportion of store card customers are employed compared to catalogue credit customers (57%) with a quarter of customers in retirement (25%). Most store card customers either own their property (37%) or have a mortgage (32%) with one fifth renting (20%). The number of customers reporting having a physical or mental condition expected to last more than 12 months was lower than for catalogue credit customers (22%).

Positive Impacts

A "point of sale ban" on extended warranties to ensure consumers have adequate tools to make a decision on whether to purchase high-cost insurance product (RTO)

19. Our analysis indicates that consumers may be paying significant costs for warranties which are sometimes of limited value, particularly when the consumer has rights to

3 https://www.citizensadvice.org.uk/Global/CitizensAdvice/Debt%20and%20Money%20Publications/Debt%20on%20your%20doorstep%20(1).pdf

repair under their standard manufacturer's warranty. Our proposals will make sure consumers are given time to reflect on whether they need these products, and limit the point of sale advantage held by firms. Our consumer research has found that many consumers are unclear about whether insurance and warranties are mandatory or optional and what additional protections they provide – or that they may have rights under standard warranties. Consumers which value the additional benefits these products may bring (faster repairs, replacements) can still opt-in to buy them. We consider that this will be to the benefit of all consumers, including those with protected characteristics – but given that so many users have protected characteristics this will have a larger positive impact on them. We have considered other options including enhanced disclosure and banning sales of warranties where consumers hold standard warranties, but we do not think disclosure alone will help consumers make informed choices when they are focused on obtaining essential goods, and we consider that a ban would be disproportionate as some consumers may value these services.

New guidance on canvassing off trade premises to ensure repeat borrowing is driven by consumers and not firms (Home-Collected Credit)

20. We are concerned that some consumers may be using home-collected credit on a longer term basis as a result of firms being able to sell further loans to consumers in their homes in the course of their regular collections. While there are some safeguards in place in both our rules and firms' policies around repeat borrowing we are consulting on new guidance clarifying that discussions on further lending are always driven by consumers and not firm representative working for the home-collected credit firms. We think this will benefit consumers by ensuring that repeat borrowing, which we consider is important to this consumer base in terms of accessing credit in order to manage unexpected expenditure, is driven by consumers and that they are not "upsold" loans. We think this will be of benefit to all consumers but will have a larger positive impact on groups with protected characteristics (in particular, gender) given so many use home-collected credit. Our proposals could also help consumers whose options are restricted by limited mobility. These consumers may place particular importance on the in-home service provided by home-collected credit and may be particularly sensitive to influence from firm representatives in an effort to preserve their relationship.

A new information remedy to ensure consumers are told the comparative costs of different types of repeat borrowing when they wish to borrow more (Home-Collected Credit)

21. This proposal will require firms to give information on the comparative costs of borrowing when consumers want to take out new loans. Refinancing (using part of a new loan to pay off an old one) is commonplace in the sector, which our evidence suggests is partly driven by consumers but may also be prioritized by firms over the issue of an additional concurrent loan. Refinancing tends to result in weekly repayments being kept low (a priority for many consumers on stretched budgets) but can be more costly overall. Consumers did not appear to be aware of the fact that this is a more expensive form of borrowing overall. We think this proposal will benefit all consumers by setting out in simple terms the difference in costs in both total cost of credit and weekly repayment terms so they are better equipped to choose the arrangement they feel is most suitable for them.

Requiring adequate explanations for BNPL and a post-contract prompt (catalogue and store cards)

22. We are concerned about the practice of catalogue and store card firms charging interest on the whole balance from the date of purchase in the event that a customer fails to repay the entire amount for BNPL. Our proposal on adequate explanations will provide clarity to consumers by requiring firms to provide detail on the circumstances when interest will become payable including the date and the rate of interest. As a consequence, consumers will be clear about the risks of taking up an offer and failing to repay within the offer period. We think this proposal will benefit all consumers but particularly benefit those who may otherwise be unable to understand the consequences of taking a BNPL offer and incur unforeseen higher interest. We also had concerns that existing consumers were not provided with a clear, timely prompt. We consider that our proposal to provide this will benefit all consumers in highlighting in advance when an offer is about to end.

Customer choice and control over credit limit increases (catalogue credit)

23. We have concerns that credit limits may be increased for catalogue credit customers without consulting them or telling them in advance. Our consumer research identified a desire amongst customers for greater choice and control to avoid the risk of temptation from credit limit increases. Our proposals to extend rules that are currently applicable to credit cards and store cards on the circumstances when a credit limit can or can't be increased will provide consumers with greater control and choice. We expect that this will benefit all consumers, in particular, those who have protected characteristics (in particular, gender) given so many use these products. The proposed rule may also address the propensity for some customers who tend to increase spending, contrary to their original intentions, when offered credit limit increases.

Treatment of customers at risk of financial difficulty (catalogue credit)

24. We have evidence that some catalogue credit customers in financial difficulties have been offered credit limit increases and want to ensure that we have appropriate protections for consumers. We also want to protect customers from interest rate increases where they are at similar risk of financial difficulties. We consider that our proposals that would extend existing rules applying to credit cards and store card firms would ensure that vulnerable consumers are protected from worsening financial situations that might arise from further spending prompted by these increases.

Earlier intervention (catalogue credit and store cards)

25. We have concerns that the flexible payments allowed on catalogue credit and store cards may mask signs of actual or possible financial difficulties that would not be identified through monitoring a customer's repayment record alone. In that case, we consider that these products warrant the same treatment identified for credit cards. We created new rules requiring firms to monitor information available to them to identify and take appropriate action to support customers at risk of financial difficulties. We expect that extending these rules to catalogue credit and store cards will directly benefit potentially vulnerable customers who are at risk of financial difficulties but who may not have missed a payment.

Persistent debt (catalogue credit and store cards)

26. We have concerns reflected in our consumer research relating to the feature common to both catalogue credit and store cards which allow for flexible payments so that customers can spread payments over a long period. One consequence of this flexibility is that customers can carry a large balance for a long time without significantly reducing their debt. We are particularly concerned that consumers may fall into persistent debt, whereby over an 18 month period, a customer may more in interest and charges than they have repaid of the principal. Our proposals to extend the rules on persistent debt that currently apply to credit cards to catalogue credit and store cards will benefit customers at different stages. At the 18 month point, it will encourage customers to consider whether they can afford to repay more quickly and so reduce their borrowing costs. At the 36 month point, firms will be required to support those who have paid a substantial amount of interest and charges but who have repaid little of the principal. We consider that these proposals will mainly benefit those likely to be in financial difficulties or at risk of developing them, including vulnerable consumers.

Negative Impacts

27. We do not think our proposals are likely to have a negative impact on protected groups. Any risks of negative impacts again fall on those groups with protected characteristics which more commonly use high-cost credit (gender, pregnancy maternity, and disability).

28. On the RTO point of sale warranties ban there is a small risk that some consumers may choose not to buy the extended warranty and may be impacted if goods break down and they have to pay for repairs, or wait longer for repairs. It is possible that some vulnerable consumers may not purchase an extended warranty which may be suitable for them as a result of the deferral. However we think that consumers should be equipped with the information and time they need to make a decision, and they can opt-in to buy the service at a later time if they wish to. They will also have some rights under standard manufacturer's warranties, although we recognise that delays in repairs could mean some consumers may go longer without essential goods. Our CBA has confirmed a net benefit to consumers as a result of these measures.

29. On RTO pricing more broadly we will need to consider any positive or negative impacts of any pricing intervention we choose to consult on in future. We will undertake an equality impact assessment as part of the work and analysis on an RTO price intervention.

30. On home-collected credit our objective is not to cut off the supply of credit but to help consumers to make better informed borrowing decisions. Our CBA has confirmed a net benefit to consumers as a result of these measures.

31. On catalogue credit our objective is not to remove access to catalogue credit and store cards to those who are not at risk of persistent debt. Whilst there is a small risk that consumers who rely on catalogue credit to buy essential goods may be impacted in meeting the persistent debt definition, we consider that the proposals on persistent debt are necessary to avoid worsening financial difficulties for these consumers. Overall, our CBA has confirmed a net benefit to consumers as a result of these measures.

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

Legislative and Regulatory Reform Act 2006 (LRRA)

We have had regard in this consultation to the principles in the LRRA and the Regulators' Code for the parts of our proposals that consist of general policies, principles or guidance. We consider that they are proportionate and result in an appropriate level of consumer protection, without creating undue burdens on firms or an adverse impact on consumers.

Annex 5
Abbreviations in this document

APR	Annual percentage rate of charge
BLF	Big Lottery Fund
BNPL	Buy now pay later
BRC	British Retail Consortium
CBA	Cost Benefit Analysis
CCA	Consumer Credit Act 1974
CCMS	Credit Card market study
CDFI	Community development finance institution
CLI	Credit limit increase
CONC	Consumer Credit Sourcebook
CP	Consultation Paper
CRA	Credit reference agency
DCMS	Department for Digital, Culture, Media and Sport
DWP	Department for Work and Pensions
EIA	Equality impact assessment
FCA	Financial Conduct Authority
FLA	Finance and Leasing Association
FS	Feedback Statement
FSMA	Financial Services and Markets Act 2000
GAP	Guaranteed Asset Protection

HCSTC	High-cost short-term credit
ICOBS	Insurance Conduct of Business Sourcebook
LRRA	Legislative and Regulatory Reform Act 2006
OFT	Office of Fair Trading
PROD 2	Product Intervention and Product Governance Sourcebook
RSL	Registered social landlord
RTO	Rent-to-Own
TAD	Theft and accidental damage

We have developed the policy in this Consultation Paper in the context of the existing UK and EU regulatory framework. The Government has made clear that it will continue to implement and apply EU law until the UK has left the EU. We will keep the proposals under review to assess whether any amendments may be required in the event of changes in the UK regulatory framework in the future.

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

All our publications are available to download from www.fca.org.uk. If you would like to receive this paper in an alternative format, please call 020 7066 9644 or email: publications_graphics@fca.org.uk or write to: Editorial and Digital team, Financial Conduct Authority, 25 The North Colonnade, Canary Wharf, London E14 5HS

Appendix 1
Draft Handbook text

CONSUMER CREDIT (HIGH-COST CREDIT AND RENT-TO-OWN) INSTRUMENT 2018

Powers exercised

A. The Financial Conduct Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):

(1) section 137A (The FCA's general rules);
(2) section 137D (FCA general rules: product intervention);
(3) section 137T (General supplementary powers); and
(4) section 139A (Power of the FCA to give guidance).

B. The rule-making provisions listed above are specified for the purposes of section 138G(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force [three months after publication] except for:

(1) Part 2 of Annex A which comes into force [day after publication]; and
(2) Parts 1, 3, 5 and 7 of Annex C which come into force [day after publication].

Amendments to the Handbook

D. The modules of the FCA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2) below:

(1)	(2)
Glossary of definitions	Annex A
Product Intervention and Product Guidance sourcebook (PROD)	Annex B
Consumer Credit sourcebook (CONC)	Annex C

Citation

E. This instrument may be cited as the Consumer Credit (High-Cost Credit and Rent-To-Own) Instrument 2018.

By order of the Board
[*date*] 2018

Annex A

Amendments to the Glossary of definitions

Insert the following new definitions in the appropriate alphabetical position. The text is not underlined.

Part 1: Comes into force [3 months from publication]

extended warranty	an agreement entered into by a *customer* for monetary consideration which provides cover, guarantees or undertakings in relation to defects in *goods*.
rent-to-own agreement	a *regulated credit agreement* which is a *hire-purchase agreement* or *conditional sale agreement* which provides for repayments to be made at intervals of less than one *month*, but excluding those in relation to *goods* acquired principally for business purposes or motor vehicles.

Part 2: Comes into force [day after publication]

retail revolving credit

a *regulated credit agreement* which is a borrower-lender-supplier agreement for running-account credit to finance the acquisition of goods or goods and services from

(1) the *lender*; or

(2) from a supplier that is in a limited network of suppliers under a direct commercial agreement with the *lender*,

and where the credit cannot be used for any other purpose, including an agreement for a store card but excluding an agreement for a credit card.

Annex B

Amendments to the Product Intervention and Product Governance sourcebook (PROD)

Comes into force on [3 months from publication]

1 Product Intervention and Product Governance sourcebook (PROD)

…

After PROD 1.4 (Application of PROD 4) insert the following new section, PROD 1.5. The text is not underlined.

1.5 Application of PROD 5

General: Who? What?

1.5.1 R *PROD* 5 applies to a *firm* which:

(1) offers to sell an *extended warranty* to a *customer*; or

(2) invites or induces a *customer* to obtain an *extended warranty* from a *person* connected to the *firm*;

in connection with the entering into of a *rent-to-own agreement* with the *firm*.

1.5.2 G A *person* connected to the *firm* includes someone who has a relevant business relationship with the *firm*.

Where?

1.5.3 R *PROD* 5 applies to a *firm* with respect to activities carried on from an establishment maintained by it, or its *appointed representative*, in the *United Kingdom*.

EEA territorial scope rule: compatibility with European law

1.5.4 R (1) The territorial scope of *PROD* 5 is modified to the extent necessary to be compatible with European law (see *PROD* 1.5.5G to *PROD* 1.5.7G for *guidance* on this).

(2) This *rule* overrides every other *rule* in *PROD* 5.

Effects of the EEA territorial scope rule

1.5.5 G The *guidance* in paragraph 2 of Part 4 of *ICOBS* 1 Annex 1 applies equally to the *rules* in *PROD* 5.

IDD, Solvency II, DMD: effect on territorial scope

1.5.6 G The *guidance* on the *IDD*, *Solvency II* and *DMD* in *ICOBS* 1 Annex 1 in relation to *ICOBS* 6A.1.4R applies equally to *PROD* 5.1.1R (to the extent that the *extended warranty* is a *contract of insurance*).

Electronic Commerce Directive: effect on territorial scope

1.5.7 G The *guidance* on the Electronic Commerce Directive in *ICOBS* 1 Annex 1, Part 4, paragraph 8 applies equally in relation to the *rules* in *PROD* 5.

…

After PROD 4 (Product governance: IDD) insert the following new chapter, PROD 5. The text is not underlined.

5 Extended warranties sold with rent-to-own agreements: customer information and deferred opt-in

5.1 Ensuring the customer can make an informed decision

5.1.1 R (1) A *firm* must give the *customer* the information in (3), at the same time and in the same *document*, when it offers to sell them an *extended warranty*.

(2) A *firm* must ensure that any other *person* to whom it has referred the *customer* gives the *customer* the information in (3), at the same time and in the same *document*, when that *person* offers to sell the *customer* an *extended warranty*.

(3) The information is:

(a) the total cost of the *extended warranty*, separate from any other prices, in the following terms:

(i) weekly;

(ii) annually; and

(iii) over the length of the *rent-to-own agreement*;

(b) the significant features and benefits, significant and unusual exclusions or limitations of the *extended warranty*, with cross-references to the relevant warranty document provisions;

(c) a statement that *extended warranties* may be available from other *persons*;

(d) an explanation of how the *extended warranty* interacts with and compares against any other products sold or offered for sale in connection with the *rent-to-own agreement* (e.g. theft and accidental damage insurance);

(e) an explanation of how the *extended warranty* interacts with and compares against any standard manufacturer's warranty that may apply to the *goods* which are the subject of the *rent-to-own* agreement, given in a way that enables the *customer* to make a clear comparison between the two;

(f) when the *extended warranty* can be concluded, as described in *PROD* 5.2.1R; and

(g) the date the information in (a) to (f) is provided to the *customer*.

(4) The information in (3) must be communicated in a way that is clear, fair and not misleading and in writing or another *durable medium*, and made available and accessible to the *customer*.

(5) This information in (3) must be drawn to the *customer's* attention and must be clearly identifiable as key information that the *customer* should read.

5.1.2 G (1) A *firm* that sells *extended warranties* that constitute *contracts of insurance* must also comply with the *rules* in *ICOBS* 6 (Product Information).

(2) *Firms* should also take into account the Supply of Extended Warranties on Domestic Electrical Goods Order 2005. Other consumer protection legislation may also be relevant.

5.2 Deferred opt-in for extended warranties

5.2.1 R (1) A *firm* must:

(a) not conclude the sale of an *extended warranty*; and

(b) ensure that no other *person* to whom the *firm* has referred the *customer* concludes the sale of an *extended warranty*;

until at least two clear *days* have passed since the required information was provided to the *customer* (*PROD* 5.1.1R).

(2) The period in (1) is one clear *day* after providing the information if the *customer*:

(a) initiates the conclusion of the sale of the *extended warranty*;

(b) consents to the conclusion of the sale of the *extended warranty* earlier than provided for in (1); and

(c) confirms that they understand the restriction in (1).

5.2.2 G For example, if a *firm* provided the required information to the *customer* on Monday, it would not (absent the *customer's* consent) be able to conclude the sale of the *extended warranty* until Thursday.

5.2.3 G Before the conclusion of the sale of an *extended warranty*, a *firm* should have regard to the information needs of its *customers* and consider whether it would be in the *customer's* interest to receive the information in *PROD* 5.1.1R again, for example, if a long time has passed between providing the information and the conclusion of the sale.

Annex C

Amendments to the Consumer Credit sourcebook (CONC)

In this Annex, underlining indicates new text and striking through indicates deleted text.

Part 1: Comes into force [day after publication]

3 Financial promotions and communications with customers

…

3.10 Financial promotions not in writing

…

3.10.3 G Firms ~~are reminded~~ should note that:

…

(3) The *FCA* takes the view that sections 48 and 49 of the *CCA* mean that any discussions about new borrowing or refinancing with a *customer*, that take place in the *borrower's* home, must be initiated by the *borrower*, either in the form of a specific written request or (but only where the *individual* is in the *borrower's* home other than for the purpose of engaging in such discussions) in the form of an oral invitation.

(4) The *FCA* has considered the potential for the use of "umbrella requests to visit". "Umbrella requests" or "permissions to call" tend to be signed by a *borrower* when entering into a *borrower-lender agreement* (or shortly after) and purport to allow the *lender* to visit the *borrower's* home to discuss other borrowing at any time over the duration of the agreement or beyond. The *FCA* takes the view that such "umbrella requests" do not meet the requirements of the *CCA*. "Umbrella requests" create open-ended opportunities for *firms* to raise the prospect of additional borrowing without the *borrower* having specifically requested or even considered it.

(5) A valid request is one made on the instigation of the *borrower* when the *borrower* wants to discuss a *borrower-lender agreement*. The *FCA* would expect to see the following for a *firm* to comply with sections 48 and 49 of the *CCA*:

(a) the request should be a positive act by the *borrower* and specifically for the purpose of discussing other borrowing;

(b) the visit should be made in response to that request. Where a request is reasonably specific on timing, the visit should be within that timing. Where the request is not reasonably specific on timing, any visit should take place within a reasonable proximity to that request for it to be clear that the visit is being made in response to that request; and

(c) there should be a separate request made for each potential agreement or contractual variation.

(6) In the *FCA*'s view this would not stop an agent or representative of a *firm* who has called on a *borrower* with the sole purpose of collecting on an existing loan from discussing additional borrowing if the *borrower* asks them do so during the collection visit. However, if the agent or representative raised the topic of additional finance, we consider it would be very difficult for them to establish that they had not visited with that purpose.

(7) We expect that *firms* should be able to rely on their existing procedures for receiving written requests from new *customers* in relation to existing *borrowers*.

Failure to comply

3.10.4 G Failure to comply with section 49 of the *CCA* is a criminal offence. Only a court can determine the meaning of sections 48 and 49 of the *CCA*.

…

Part 2: Comes into force on [3 months from publication]

4 Pre-contractual agreements

…

4.2 Pre-contract disclosure and adequate explanations

…

Adequate explanations in relation to particular regulated credit agreements.

4.2.15 R The following information must be provided by the *lender* or a *credit broker* as part of, and in addition to that provided under, the adequate explanation required by *CONC* 4.2.5R, where applicable, in the specified cases:

(1) for *credit token agreements*:

…

(e) except in relation to *retail revolving credit*, the limitations on any zero percentage or low interest or other introductory offer; and

…

(3A) for a *home credit loan agreement* that would refinance an existing *home credit loan agreement* and also an involve an increase in the amount of principal outstanding, and where an alternative option could be entering into a separate *home credit loan agreement* with that lender for the amount of the additional principal, the information must include an explanation of the difference in costs, if any, between the weekly amount payable and the total amount repayable for a refinanced loan as opposed to the situation where the *borrower* enters into a separate, concurrent loan. If the regular period after which the next payment is due is not weekly but a different period, then the lender must refer to that other period.

…

(7) … ;

(8) for *retail revolving credit*, the limitations that apply to any zero percentage or low interest, introductory or other promotional offer, including the circumstances in which interest could become payable and how it would be calculated if those circumstances arose, including the date from which interest would accrue, the rate of that interest and the amount of principal on which the interest would be charged. If, for example, failing to meet the conditions for the application of the offer would result in interest being charged at a higher rate, or from the date of the purchase of the *goods* or services or on the total purchase price of the *goods* or services without account being taken of *repayments* made during the offer period, this must be included in the adequate explanation.

…

…

4.2.16 G (1) Where a *customer* does not have a good understanding of the English language, the *lender* or *credit broker* may need to consider alternative methods of providing relevant information concerning the explanation required by *CONC* 4.2.5R in order for the *customer* to make an informed decision, such as, providing the information to a person with such understanding who can assist the *customer*, for example, a friend or relative.

[**Note**: paragraph 3.4 (box) of *ILG*]

(2) The explanation in *CONC* 4.2.15R(3A) should enable a *customer* to easily understand the different costs of refinancing as opposed to keeping the existing loan and taking out an additional concurrent loan, for example by indicating whether total amounts payable are

higher or lower.

…

6 Post contractual requirements

…

Part 3: Comes into force [day after publication]

6.7 Post contract: business practices

Application

6.7.1 R …

(4) *CONC* 6.7.2R to 6.7.3G do not apply to *retail revolving credit*.

…

Business practices: credit cards and retail revolving credit

6.7.3A R A *firm* must monitor a *retail revolving credit customer's* or a credit card *customer's* repayment record and any other relevant information held by the *firm* and take appropriate action where there are signs of actual or possible financial difficulties.

6.7.3B G (1) Circumstances in which there are signs of actual or possible financial difficulties include where there is a significant risk of one or more of the matters set out in *CONC* 1.3.1G(1) to (7) (Guidance on financial difficulties) occurring in relation to the *retail revolving credit customer* or credit card *customer*.

…

…

Credit card and ~~store card~~ retail revolving credit requirements

…

6.7.7 R A *firm* must not increase, nor offer to increase, the *customer's credit limit* on a credit card ~~or store card~~ or *retail revolving credit* agreement where:

…

Part 4: Comes into force [3 months from publication]

6.7.8 R A *firm* under a *retail revolving credit* agreement, or a *regulated credit agreement* for a credit card, ~~or a store card~~ must:

…

6.7.9 R A *firm* under a *retail revolving credit* agreement, or a *regulated credit agreement* for a credit card, ~~or store card~~ must notify the *customer* of a proposed increase in the *credit limit* under the agreement at least 30 days before the increase comes into effect, except where:

…

Part 5: Comes into force [day after publication]

6.7.10 R Where a *customer* is at risk of financial difficulties, a *firm* under a *retail revolving credit* agreement or a *regulated credit agreement* for a credit card ~~or store card~~ must, other than where a promotional rate of interest ends, not increase the rate of interest under the agreement.

…

…

Part 6: Comes into force [3 months from publication]

6.7.16A R (1) This *rule* applies only to *retail revolving credit* agreements to which Part 6 of the *Payment Services Regulations* does not apply.

(2) Where a *customer* has the benefit of a zero percentage or low interest, introductory or promotional offer that depends on the *customer* meeting certain conditions, a *firm* must provide notice to the *customer* reminding them of any action they need to take to meet the conditions of the offer and the date by which such action must be taken, within a reasonable period before that date, taking account of the time at which the information may be most useful to the *customer*.

This notice must be provided in an appropriate medium (taking into account any preferences expressed by the *customer* about the medium of communication between the *firm* and the *customer*), in plain language and sufficiently prominent, so that it is likely to be seen and understood by the *customer*.

…

Credit cards and retail revolving credit: persistent debt

…

Part 7: Comes into force [day after publication]

6.7.27 R (1) This *rule* applies to a *firm* with respect to communicating with a *customer* about, and receiving payments or exercising rights under, a ~~credit card agreement~~ *regulated credit agreement* for a credit card or *retail revolving credit*, if the *firm* assesses that the amount the *customer* has paid to the *firm* towards the credit card balance or *retail revolving credit* balance over the immediately preceding 18 *month* period comprises a lower amount in principal than in interest, fees and charges.

…

(3) The *rule* in paragraph (1) does not apply:

(a) where the balance on the credit card or under the *retail revolving credit* agreement was below £200 at any point in the 18 month *period*; or

(b) where the *firm* has sent a communication to the *customer* in accordance with paragraph (4) in the preceding 18 *months* in relation to the credit card or *retail revolving credit* facility; or

…

(4) Where the *rule* in paragraph (1) applies in relation to a credit card *customer* or a *retail revolving credit customer*, a *firm* must, in an appropriate medium (taking into account any preferences expressed by the *customer* about the medium of communication between the *firm* and the *customer*) and in plain language:

…

6.7.28 G (1) For the purposes of *CONC* 6.7.27R, *CONC* 6.7.30R, *CONC* 6.7.34G, *CONC* 6.7.39R and *CONC* TP 8,“principal” comprises only the amount of *credit* drawn down by the *customer* under the credit card agreement or *retail revolving credit* agreement, and does not include any interest, fees or charges added to the account.

…

6.7.29 R (1) This *rule* applies in respect of a credit card *customer* or a *retail revolving credit customer* to whom a *firm* is required to have sent a communication under *CONC* 6.7.27R(4).

…

6.7.30 R (1) This *rule* applies:

(a) in respect of a credit card *customer* or *retail revolving credit customer* to whom a *firm* is required to have sent a communication under *CONC* 6.7.27R (1); and

(b) where the amount that the *customer* has paid to the *firm* towards the credit card or *retail revolving credit* balance, over the 18-*month* period immediately following the date on which the requirement to send a communication under *CONC* 6.7.27R(1) arose, comprises a lower amount in principal than in interest, fees and charges.

(2) This *rule* does not apply:

(a) where the balance on the credit card or *retail revolving credit* was below £200 at any point in the 18-*month* period;

(b) to any part of the balance on the credit card or *retail revolving credit* that has previously been subject to the requirements of paragraph (3).

(3) A *firm* must take reasonable steps to assist a *customer* who falls under paragraph (1) to repay the balance on their credit card or *retail revolving credit* as it stands at the end of the period specified in that paragraph more quickly and in a way that does not adversely affect the *customer's* financial situation.

…

6.7.31 R Where a *firm* is required to assist a *customer* to repay more quickly under *CONC* 6.7.30R(3), a *firm* must contact the *customer* to:

…

(4) inform the *customer* that if the *firm* does not receive a response to the request under paragraph (3) in the time specified, the *firm* will suspend or cancel the use of the credit card or *retail revolving credit* facility.

6.7.32 G (1) The options a *firm* may set out under *CONC* 6.7.31R(3) in relation to a credit card or *retail revolving credit* include, for example, increasing the amount of *monthly* payments ~~on the credit card~~ under a repayment plan, or transferring the balance ~~on the credit card~~ to a fixed-sum unsecured personal loan.

…

6.7.33 G …

(2) The *FCA* expects a "reasonable period" under paragraph (1), *CONC*

6.7.37R and *CONC* 6.7.38G for credit cards and store cards to usually be between three and four years. Only in exceptional circumstances should the repayment period extend beyond four years; and even in such cases, the extension should not be significant and there should be no additional cost to the *customer* as a result of the repayment period extending beyond four years. In relation to *retail revolving credit* other than store cards, the *FCA* expects a "reasonable period" to usually be approximately two years.

6.7.34 G References in *CONC* 6.7.27R, *CONC* 6.7.31R(3) and *CONC* 6.7.32G(1) to a *customer* increasing payments to the *firm* include circumstances where the amount a *customer* pays remains fixed at the same amount the *customer* was previously paying but, assuming there is no further spending ~~on the card~~ on the account, represents an increase in the percentage of the outstanding principal that is repaid each *month* as the balance reduces.

6.7.35 R (1) Where a *customer* does not respond to a *firm's* request under *CONC* 6.7.31R(3), a *firm* must, at the end of the period specified in the request, suspend or cancel the *customer's* use of the credit card or *retail revolving credit* facility.

(2) Where a *customer* confirms that one or more of the options proposed under *CONC* 6.7.31 R(3) is *sustainable*, but states that they will not make the increased payments, a *firm* must suspend or cancel the *customer's* use of the credit card or *retail revolving credit* facility.

(3) Where a *firm* suspends the *customer's* use of the credit card or *retail revolving credit* facility under paragraph (1) and the *customer* subsequently responds to the *firm's* request under *CONC* 6.7.31R(3), the *firm* may withdraw the suspension if this would be in line with the other provisions in this section.

6.7.36 G Where a *firm* suspends or cancels the *customer's* use of the credit card or *retail revolving credit* facility under *CONC* 6.7.35R the *firm* is not, unless the *customer* responds to the *firm's* request under *CONC* 6.7.31R(3), required to take further steps under *CONC* 6.7.37R to *CONC* 6.7.39R. *Firms* are however reminded of *CONC* 6.7.3AR, which requires *firms* to take appropriate action where there are signs of actual or possible financial difficulties, and *CONC* 7.3.4R, which requires *firms* to treat *customers* in default or arrears difficulties with forbearance and due consideration.

…

6.7.38 G …

(2) The *FCA* expects that it will generally be necessary for *firms* to suspend or cancel the use of the credit card or *retail revolving credit* facility of a *customer* that the *firm* is required to treat with forbearance under *CONC* 6.7.37R with a view to ensuring the *customer* repays the outstanding balance in a reasonable period. This expectation does not apply, however, where the suspension or

cancellation of use of the ~~credit~~ ~~card~~ facility would cause a significant adverse impact on the *customer's* financial situation, for example where the *customer* depends on the ~~credit~~ ~~card~~ facility for meeting essential living expenses (such as in relation to a mortgage, rent, council tax, food bills and utility bills) or the purchase of essential items (which may include but is not limited to items such as school uniform, baby essentials or a refrigerator). Equally, the *FCA* considers that it will generally not be appropriate to withdraw the suspension of the use of a *customer's* credit ~~card~~ facility under *CONC* 6.7.35R(3) if the *firm* is required to treat the *customer* with forbearance under *CONC* 6.7.37R.

6.7.39 R Where a *firm* does not suspend or cancel the use of the credit card or *retail revolving credit* facility of a *customer* falling under *CONC* 6.7.30R, the *firm* must take reasonable steps to ensure that the *customer* does not, in the 18-*month* period immediately following, repay an amount to the *firm* towards the credit card or *retail revolving credit* balance that comprises a lower amount in principal than in interest, fees and charges in relation to any spending on the ~~card~~ facility in this period.

After CONC TP 7A (Transitional provisions in relation to the Consumer Credit (Earlier Intervention and Persistent Debt) Instrument 2018 insert the following new transitional provisions. The text is not underlined.

(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**
	Material to which the transitional provision applies		**Transitional provision**	**Transitional provision: dates in force**	**Handbook provision: coming into force**
7B.1	*CONC* 6.7.1(4)R, *CONC* 6.7.3AR to *CONC* 6.7.3DG and *CONC* 6.7.27R to *CONC* 6.7.40G	R	A *firm* may comply with *CONC* as if the changes made by the Consumer Credit (High-Cost Credit and Rent-to-Own) Instrument 2018 had not been made until (but not including) [date 6 *months* from publication]. But where a *firm* elects, in relation to *retail revolving credit*, to comply before that date with *CONC* as amended by that Instrument, it must comply	[date]	[date]

			with the relevant provisions in full. Consequently, the time periods set out in the *rules* to which this transitional provision applies are to be determined by reference to the date on which the *firm* first acted in compliance (or purported compliance) with those *rules*.		
7B.2	*CONC* 6.27R to *CONC* 6.40G	G	The effect of TP 7B.1 is that no later than [date – six *months* after publication] *firms* must start to look back at the repayment records for *retail revolving credit customers* over the preceding 18-*month* period and identify any *customers* that fall within the application of *CONC* 6.7.27R (and must thereafter continue to do so on at least a *monthly* basis). *Firms* must then send those *customers* a communication in accordance with *CONC* 6.7.27R (3). Between 9 and 10 *months* after this communication is required to be sent, *CONC* 7.7.29R requires *firms* to take the additional steps set out in that *rule* with respect to that group of *customers*. 18 *months* after this CONC 6.27R communication is required to be sent, CONC 6.7.30R to CONC 6.7.40G potentially require the *firm* to take the further steps described in those *rules* in relation to that group of *customers* where *CONC* 6.7.30R applies. *CONC* 6.7.30R applies only where the amount that *customer* has paid to the *firm* towards the balance on the *retail revolving credit* account, over the 18-*month* period		

			following the date on which the *CONC* 6.7.27R communicated was triggered, comprises a lower amount in principal than in interest, fees and charges. This means that the earliest date on which a firm may have obligations under *CONC* 6.7.30R is [date] (except as mentioned below). However, *firms* are not required to delay implementation to the end of the six-*month* period set out in TP 7B.1: where a *firm* takes a step in compliance with one of the *rules* in question before [date] in relation to a particular *retail revolving credit agreement* (for example, carrying out the 18-*month* review), the time for taking subsequent steps required to be taken under those *rules* is to be determined by reference to the date of that first step, and not by reference to [date] (or some later date).		

Appendix 2
Draft non-Handbook Guidance for consultation

Helping tenants find alternatives to high-cost credit and what this means for social housing landlords

We want to support and encourage referrals when consumers need credit and consider that in this area social landlords can play a key role in assisting tenants find alternatives to high-cost credit when looking to obtain essential household goods.

Some first-time tenants moving into unfurnished accommodation may not possess essential goods or domestic appliances. In such cases, understanding that there are options in addition to high-cost credit will be likely to assist tenants.

If you are a social landlord and want to assist tenants find alternatives to high-cost credit, there are some things that you can do that would not constitute regulated activity and so not require authorisation from the FCA. Here's a quick guide.

We consider that if you suggest that a tenant consider approaching a local credit union or Community Development Finance Institution (CDFI) and do no more than this, you are unlikely to be credit broking. This could include providing content on your website that explains what these institutions are and why they might provide an alternative to high-cost credit for your tenants.

If you are otherwise currently referring tenants or planning to do so and your activities do not fall into the above scenario, such as where you provide tenants with contact details of specific providers, you are likely to be engaged in credit broking and need FCA authorisation.

We recognise that making an assessment on whether you are credit broking can be difficult. We want to help make this easier and so we have set up a specialist team that can provide individual guidance to social landlords. You can contact them at the following email address: RSL@fca.org.uk.

Where you want to offer more services or partner with other organisations, you will probably need to be authorised. We have prepared a guide to the authorisation process for social landlords that explains what you need to do and what assistance we can provide to make this a straightforward process.

[We will provide a link to the RSL guidance that we are consulting on and is below].

Guidance consultation

Helping tenants find alternatives to high-cost credit and what this means for social housing landlords

May 2018

1 Introduction

1.1 This document aims to assist social housing landlords, including local authorities and housing associations, to understand the scope of regulation when they help tenants to find alternatives to high-cost credit. These alternatives could be from credit unions or Community Development Finance Institutions (CDFIs), for example.[1]

1.2 We recognise that the social housing model may contribute to some tenants turning to high-cost credit as they are required to move promptly into new accommodation and in some circumstances make quick decisions on how to acquire essential furniture. Moving with such short notice may have cost implications for tenants and put the most vulnerable at risk, particularly those who may not possess essential household goods. In such circumstances, understanding that there are alternatives to high-cost credit will be likely to assist tenants.

1.3 We want to support and encourage referrals when consumers need credit and consider that in this area social landlords can play a key role in assisting tenants find alternatives to high-cost credit when looking to obtain essential household goods. This would foster better options for consumers and could provide them with a cheaper, lower-risk source of finance. Social landlords may also be able to support tenants in sourcing goods on hire.

Who does this guidance apply to?

1.4 This guidance applies to registered social landlords; including housing associations and housing charities.

1.5 Note that local authorities are excluded from most credit-related regulated activity, including credit broking, debt counselling and debt adjusting.[2]

2 Making referrals

2.1 We want to encourage social landlords to help tenants find alternatives to high-cost credit. There are many things a landlord can do that, depending on the circumstances of the case, may individually or collectively constitute credit broking. Credit broking is an activity that is regulated by the FCA.

1 https://www.fca.org.uk/publication/feedback/high-cost-credit-review-update.pdf at paragraphs 4.23-4.25
2 See our Perimeter Guidance ('PERG') PERG 2.9.23G for guidance on the exclusion for local authorities in Article 72G of The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 https://www.handbook.fca.org.uk/handbook/PERG/2/9.html

Example
Some of your tenants moving into unfurnished properties do not possess essential household goods and furniture such as a bed or fridge. You wish to provide assistance.

For example, you might

- refer a tenant to a credit provider such as a local credit union / CDFI
- refer a tenant to a provider of goods on hire
- refer a tenant to a credit broker
- provide details to the tenant for contacting the provider or broker
- take the lead in calling the lender or set up a meeting on the tenant's behalf

Any of the above is likely to be credit broking.

Credit broking

2.2 When referring tenants to sources of credit or hire or other credit brokers, you are likely to be engaged in 'credit broking'. If as a social landlord you are currently doing this or planning to do so you will need FCA authorisation.

What this means for you

2.3 Whether or not an activity involves credit broking will depend upon the individual facts and circumstances. Our perimeter guidance (PERG) explains the various activities that fall within credit broking in more detail at PERG 2.7.[3]

2.4 It is very important to note that the fact that you may not receive a fee or commission for providing details or referring your tenants to sources of credit or hire does not necessarily mean that you will not be credit broking.

2.5 As a social landlord, we recognise that making an assessment on whether you are credit broking can be difficult. We want to help make this easier and so we have set up a specialist team that can provide individual guidance to social landlords. You can contact them at the following email address: RSL@fca.org.uk. It is important that you do contact us even if you are not sure if you are credit broking as it is a criminal offence to engage in credit broking if you are not authorised or have a relevant exemption.

2.6 If you do contact us, we can give you the most help if you can provide full details of the activities you undertake when helping tenants find alternatives to high-cost credit. Please state how (and how often) this is done and whether it involves specific providers.

3 Authorisation process

3.1 If you are engaged in regulated activity, you will need authorisation from the FCA. You will not need authorisation if your activity is covered by a relevant exclusion (for example, a local authority) or you are an appointed representative of an authorised person.

3 https://www.handbook.fca.org.uk/handbook/PERG/2/7.html

3.2 We will do all we can to assist you in the application process and have set up a specialist authorisation team to assist. The team will assess your application by considering the size and nature of the regulated activity (credit broking) that you do and the potential risks to consumers.

3.3 The additional information below, will help you understand the authorisation process. You might also like to be aware of the possible options of:

- **acting as an appointed** representative for a credit union or CDFI you wish to refer tenants to (see appointed representatives text box below)
- **applying for limited permission** if you are only intending to refer tenants to providers in relation to hire or hire-purchase agreements and will not engage in any other regulated activity (see full or limited permission section below)

3.4 To assist you there is a summary of the process for applying for authorisation on our website – see https://www.fca.org.uk/firms/authorisation/how-to-apply.

Getting ready for authorisation

3.5 There is an online checklist for the main things you need to do before applying to us for authorisation - https://www.fca.org.uk/firms/authorisation/how-to-apply/consumer-credit.

3.6 You would have to submit an application, but this would only have to focus on how you meet our standards in relation to the activity you are carrying on.

3.7 Where there are no charges to consumers and no remuneration paid by the provider to the broker, credit broking is likely to be a relatively low risk activity since there is very little risk of people being driven to unaffordable or inappropriate sources of finance in order to make the broker more money.

3.8 Your application would be dealt with by a team of specialists. They can provide you with all the help you need and make the process as smooth as it can be.

3.9 Our online checklist for credit firms seeking authorisation when commencing preparation for authorisation may also help - see https://www.fca.org.uk/firms/authorisation/how-to-apply/consumer-credit.

Business plan
As a social landlord you may wish to consider including in your business plan:

- The legal status of your organisation
- Your primary business purpose, e.g. social housing
- Why you want to carry out regulated activities, i.e. credit broking
- The customer base of these regulated activities, e.g. what types of tenants, on what scale and how they will be identified
- The services you provide and any areas you specialise in
- How your organisation is set up and governed
- The background and experience of everyone performing significant influence controlled functions[4]
- Your long term strategy and your financial plans
- Your experience of regulated activities including any existing permissions you already hold

3.10 If you would like us to review your documents or to discuss them ahead of making an application, we would be happy to assist. You can email our specialist team at RSL@fca.org.uk.

3.11 We will also ask you to demonstrate how your organisation meets our requirements including our minimum conditions, known as Threshold Conditions, which all firms must meet to be authorised. Guidance on the Threshold Conditions is provided in our Handbook[5] and summarised in our Guide for Consumer Credit Firms.[6] Our dedicated team would be happy to discuss the Threshold Conditions and how they may apply to you using the following email address: RCL@fca.org.uk

Once you are ready to apply, what do you need to do?

3.12 You will need to complete your application on Connect, our online system.[7] We will assess your application to see if you meet the standards we require. We have a statutory duty to make a decision within:

- 6 months of receiving your completed application
- 12 months of receiving an incomplete application (or 6 months from when an incomplete application becomes complete)

However, in practice we are likely to process your application much more quickly.

3.13 If your application is incomplete or needs further explanation, we will ask you to clarify it or provide further information or documentation. For example, there may be inconsistent or missing answers.

4 More information is provided in our guide for consumer credit firms https://www.fca.org.uk/publication/finalised-guidance/consumer-credit-being-regulated-guide.pdf
5 https://www.handbook.fca.org.uk/handbook/COND.pdf
6 https://www.fca.org.uk/publication/finalised-guidance/consumer-credit-being-regulated-guide.pdf
7 Our online application system, Connect: https://www.fca.org.uk/firms/connect

3.14 If you need to apply for full permission we will need more details about your business than if you apply for limited permission. A list of full permission activities is provided in our guide for consumer credit firms.[8]

3.15 We recognise that this may be an unfamiliar process, particularly where regulated activity is not a primary function. However, we can assist to make this a straightforward process.

3.16 We have set up a team of specialists within our Authorisations Department, who are familiar with applications from social landlords. They will provide you with the help you need.

Full or limited permission

3.17 We have two categories of authorisation for consumer credit firms:

- 'limited permission'
- 'full permission'

3.18 If you need to apply for full permission, you will be subject to more checks and have more conditions to meet during authorisation and when you carry out credit-related regulated activities.

3.19 Applying for limited permission is restricted to certain activities. In your role as a social landlord it may include the limited permission activities of recommending providers who can offer regulated consumer hire or hire-purchase agreements.[9]

3.20 If you wish to discuss these activities further you can use the dedicated email address and we will be happy to assist: and we will be happy to assist: RSL@fca.org.uk.

3.21 The fee for limited permission credit broking where your activity is not for profit is £100 (we would be happy to discuss if this applies to you).

3.22 As part of the consideration of whether limited permission is applicable, you will also be asked if you have acted as lender in relation to credit agreements or mortgages. In particular, whether you have a back-book of second-charge loans entered into before April 2014. If you do, it is likely that you will need permission for exercising, or having the right to exercise, a lender's rights and duties under a regulated credit agreement. This requires full permission and will necessitate an additional application fee. If you have any questions about this, please use the dedicated email address RSL@fca.org.uk.

Appointed representatives

3.23 One method by which social landlords may adopt a more streamlined approach to authorisation is to become an appointed representative of an alternative lender. This can have advantages and disadvantages which are set out in the text box below.

8 https://www.fca.org.uk/publication/finalised-guidance/consumer-credit-being-regulated-guide.pdf
9 In the former, the agreement is regulated since it is capable of lasting more than 3 months. In the latter, it is regulated because of the option to purchase at the end of hire.

Appointed representatives

An appointed representative is a firm that carries on regulated activities under the supervision of another firm that we authorise. If you wish to make referrals to a certain credit union or CDFI, you may wish to explore with them whether they would be willing to assist you by taking on the role of principal with you acting as their appointed representative.

This would require an agreement between you and the credit union or CDFI. Under this agreement, they would be responsible as the principal for ensuring that you meet our requirements. We would not have a direct relationship with you as the appointed representative.

However, it requires certain formalities:

- There must be a written contract between the credit union or CDFI as the principal and you as an appointed representative that sets out the arrangement between you in writing
- The credit union or CDFI would have to take full responsibility for ensuring that you comply with our rules
- Before entering into an agreement with you, they will need to carry out sufficient checks to ensure you are financially stable and that they have achieved, and are maintaining, a satisfactory level of competence

As an appointed person you will also need to understand and comply with regulatory requirements relating to the credit broking.

If you are in doubt, we strongly suggest you apply for permission but welcome enquiries from social landlords for individual guidance. You can send enquiries to our dedicated team using this email: RSL@fca.org.uk.

Approved persons and controlled functions

3.24 Once you are authorised you will also have to meet requirements on 'approved persons'. An approved person is an individual we approve to perform 'controlled functions'. The controlled functions are important considerations in well-run businesses and, emphasise the role of senior staff and others for overseeing compliance with rules and legislation.

3.25 The number and type of approved persons you require depend on what you do and the legal status of your business. Entities engaged in credit broking usually only need one approved person. This person would be responsible for ensuring the firms' consumer credit activities are carried out in a compliant manner. They also act as our point of contact within the business.

3.26 We provide more information on approved persons in our guide for consumer credit firms.[10] If you have any questions about approved persons or controlled functions we would be happy to assist. You can email our dedicated team at RSL@fca.org.uk.

What happens when I am authorised?

3.27 Once you are authorised you will be regulated by the FCA. This means you will have to meet our standards at all times. If we are told (or find out) that you are not meeting our standards we will take action to put things right.

10 https://www.fca.org.uk/publication/finalised-guidance/consumer-credit-being-regulated-guide.pdf

3.28 If the people registered as Senior Managers have done something wrong we can take action against them. We provide more information on this in our guide for consumer credit firms.[11]

3.29 Regulated firms also have to pay fees and report certain information to us.

3.30 You will also have to report certain information to us on an annual basis. For credit broking, this information is limited to your annual revenue, how it is obtained, and the total number of customers and transaction in the year.

Fees

3.31 We are funded by the firms we regulate through fees. We aim to cover our costs in a way that is as fair and efficient as possible.

3.32 Firms have to pay a fee when they apply for authorisation and then annual fees for every year they are authorised.

3.33 The fee that a firm has to pay will be proportionate to the size of the firm's business and the type of authorisation. Credit brokers that generate no income from their broking activity currently pay £303 per year. If you make money by broking credit this fee will change.

3.34 Firms that can benefit from limited permission will have lower fees than those of higher-risk firms that need full permission.

3.35 We are also the registering authority under the Cooperative and Community Benefit Societies Act 2014 and Cooperative and Community Benefit Societies Act (Northern Ireland). To become a registered society, applicants must register with us. Many social landlords will already be registered with us and this is separate to the issue of whether your society wishes to carry out a regulated society. There is a one-off fee to register your society and we also charge a yearly fee, which is based on your society's total assets.

3.36 More information about application and annual fees is available on our website.

11 https://www.fca.org.uk/publication/finalised-guidance/consumer-credit-being-regulated-guide.pdf

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FINANCIAL
CONDUCT
AUTHORITY

25 The North Colonnade Canary Wharf London E14 5HS
Telephone: +44 (0)20 7066 1000
Website: www.fca.org.uk