
FURTHER FIRST SUPERVISORY NOTICE

To: **Indigo Michael Limited**

Reference Number: **715525**

Address: **Windsor Court
Kingsmead Business Park
Frederick Place
High Wycombe
Buckinghamshire
HP11 1JU**

Date: **15 December 2022**

1 ACTION

- 1.1 For the reasons given and pursuant to sections 55L(2)(a), 55L(2)(c) and (3)(b) of the Financial Services and Markets Act 2000, the Financial Conduct Authority has decided to vary the requirements imposed on Indigo Michael Limited by a First Supervisory Notice issued on 12 July 2022 so that:

Requirement 1: Assumptions applied to creditworthiness assessment

- 1) Before taking on new customers or offering credit limit increases to existing customers, IML must, when conducting its creditworthiness assessment assume that repayment of the full capital balance plus interest will be collected, without the customer having to borrow to meet repayments, when the relevant conditions to collect such a repayment are met.
- 2) Should IML consider that it is not reasonable to apply this assumption in the circumstances of the case, IML must record the rationale for its decision in writing and limit its use of a CPA to a maximum of the monthly sum it has

assessed the customer is able to repay within its creditworthiness assessment (defined as the "Monthly Reasonable Repayment Amount").

Requirement 2: Use of continuous payment authority

- 3) IML must not use a CPA to take repayments from any existing customers where IML has reason to believe there are insufficient funds in the account, or that taking payment would leave insufficient funds for priority debts or other essential living expenses, leading to the customer borrowing further from IML or another firm, or entering their overdraft facility to meet such expenses.
 - 4) IML must not use a CPA to take repayments greater than the Monthly Reasonable Repayment Amount that it has assessed a customer can afford to repay in its creditworthiness assessment or, if lesser, 50% of the customer's monthly net disposable income. In particular, IML must not use a CPA to take repayment of the full capital balance plus interest when the relevant conditions for doing so are met unless IML has assessed the customer's ability to make such a repayment when conducting its creditworthiness assessment and has reasonably determined that a customer will have sufficient funds to make the repayment and be left with sufficient funds for priority debts and other essential living expenses.
 - 5) IML must make customers aware of this change in approach and remind them that additional manual payments can be made to minimise the interest payable. Where the change in approach means a customer may miss a minimum repayment, IML should contact the customer explaining why the CPA has not been used and invite them to make a payment or offer forbearance as appropriate.
 - 6) IML should articulate to new and existing customers in a clear and transparent manner that, if determined affordable, it will seek to collect the full capital balance plus interest when the relevant conditions for doing so are met. This information should be communicated, but is not limited to the following, during the application stage, in the documentation provided to customers at application and in the monthly statement sent, on IML's website and through IML's dashmail system or other processes used for providing updates to customers.
- 1.2 The Requirements shall take immediate effect and remain in force unless and until varied or cancelled by the Authority (either on the application of IML or of the Authority's own volition).

2 REASONS FOR ACTION

Summary

- 2.1 The Authority has concluded, on the basis of the facts and matters described below that it is appropriate to exercise its power under section 55L(2) and (3) of the Act to impose the Requirements on IML because it is desirable in order to advance the Authority's operational objective of securing an appropriate degree of protection for consumers (section 1C of the Act).
- 2.2 The Authority has serious concerns relating to IML's business in that it appears to be operating in potential breach of Principle 6 (Customers' interests):
 - 1) When conducting its creditworthiness assessment, IML assumes a customer will repay the full capital balance plus interest in equal instalments over three

or four months depending on the product, up to 50% of the customer's monthly net disposable income. In practice, IML has a contractual right to collect sums greater than the minimum monthly or Monthly Reasonable Repayment Amount that it has assessed the customer can afford, including in one collection. The Authority is concerned that IML may place consumers at risk of being made to repay debt at a rate quicker than they can afford.

2) IML monitors a customer's bank account and uses a CPA to collect repayments automatically of up to the full amount owed in outstanding capital and interest when relevant conditions are met. The Authority is concerned that this practice may leave the customer with insufficient funds to meet priority debts or other essential living expenses, as well as lead the customer to borrow further from IML or another firm, or to enter their overdraft facility to meet such expenses.

2.3 The Authority considers that imposition of the Requirements should take immediate effect because the matters set out in this First Supervisory Notice casts serious doubts that IML is treating customers fairly.

3 DEFINITIONS

3.1 The definitions below are used in this First Supervisory Notice:

"the Act" means the Financial Services and Markets Act 2000;

"the Authority" means the Financial Conduct Authority;

"CONC" means the detailed obligations set out in the Consumer Credit sourcebook of the Handbook that are specific to credit related regulated activities;

"CPA" means continuous payment authority;

"Handbook" means the Authority's online handbook of rules and guidance (as in force from time to time);

"IML" means Indigo Michael Limited;

"Monthly Reasonable Repayment Amount" means the maximum monthly sum that IML has assessed is reasonable for the customer to repay and can afford based on repayment of the full capital balance plus interest in equal instalments over three months for SafetyNet or four months for Tappily, up to 50% of the customer's monthly net disposable income;

"Principle" means the Authority's Principles for Businesses which are general statements of the fundamental obligations of firms under the regulatory system;

"Requirements" means the terms set out in section 1.1 above;

"Supervision" means the Authority's Supervision Division; and

"Tribunal" means the Upper Tribunal (Tax and Chancery Chamber).

4 FACTS AND MATTERS

Background

4.1 IML was authorised with full permission on 25 August 2016 to operate as a credit

broker and lender. It is permitted to undertake the regulated activities of credit broking, entering into regulated credit agreement as lender and exercising lender's rights and duties under a regulated credit agreement.

- 4.2 IML has also been an authorised payment institution since 4 June 2020 with permission to provide payment services.

Failings and risks identified

Running account credit agreements

- 4.3 IML operates in the high-cost lending sector, trading as SafetyNet and Tappily. Both products are deemed running account credit facilities, meaning the credit agreements have no fixed or minimum duration. Running account credit is a financial facility under a credit agreement through which the borrower is able to receive from time to time from a lender cash up to a certain credit limit.
- 4.4 According to IML, SafetyNet and Tappily are designed for meeting short term credit requirements as they arise and can be used by borrowers to smooth their income and expenditure flows over time. They are not suitable for paying other debts or anyone struggling to control their finances, and neither are they designed to be used for a one-off credit requirement for a fixed term.
- 4.5 The products operate in a similar way, although there are some notable differences such as in the minimum monthly repayments, repayment periods, how long interest is applied to balances and the level of repayment caps that can be set.

SafetyNet

- 4.6 SafetyNet enables a customer to borrow money up to their credit limit. Once repaid, the funds are available to borrow again. SafetyNet offers the customer a revolving line of credit with a limit of up to £1,000. The product also has a "Smart Top Up" feature that enables the customer to top up their nominated bank account keeping it above the agreed SafetyNet Level for further draw down.
- 4.7 The customer must repay the minimum monthly amount by the date specified in each monthly statement sent. The minimum monthly repayment is 5% of the outstanding balance subject to a minimum of £20, or the outstanding balance if it is less than £20.
- 4.8 Unless otherwise agreed, whilst the customer has an outstanding balance and IML has a connection to the customer's nominated bank account, it will attempt to take an automatic repayment each time money comes into the bank account. This is subject to the following conditions:
- 1) IML will only ever take a repayment when the balance on the bank account is higher than the SafetyNet Level. The SafetyNet Level is set by the customer being an amount between £0 and £500. Where the customer has not pre-set a SafetyNet Level, the default SafetyNet Level will be set at £20 above their overdraft limit.
 - 2) Whenever IML takes an automatic repayment, it will always leave the balance of the bank account at least £30 above the SafetyNet Level to avoid triggering a Smart Top Up drawdown of credit.
 - 3) The automatic repayment amount will be the full amount owed by the customer in outstanding capital and interest.

- 4) The minimum amount of money being paid into the bank account which will trigger an automatic repayment to IML is £50. If the balance owed is less than £50, IML may take the full amount owed on a lesser amount being paid into the bank account.

4.9 Interest will be charged on the balance outstanding at a rate of 0.8% per day variable (equating to 32% per annum) for each day during which the customer has a balance outstanding whether for all or part of that day. Interest will be charged on each drawdown of credit for a maximum of 40 days from the date of drawdown.

Tappily

4.10 Tappily offers a customer a revolving line of credit with a limit of up to £2,500 to borrow as and when needed. The product monitors the customer's nominated bank account and when their balance drops to a pre-agreed Protection Level, an "auto borrowing" feature enables Tappily to automatically transfer funds into the bank account.

4.11 The customer must repay the minimum monthly amount by the date specified in each monthly statement sent. The minimum monthly repayment is 5% of the outstanding balance subject to a minimum of £100, or the outstanding balance if it is less than £100.

4.12 Unless otherwise agreed, whilst the customer has an outstanding balance and IML has a connection to the customer's nominated bank account, it will attempt to take an automatic repayment each time money comes into the bank account. This is subject to the following conditions:

- 1) IML will only ever take a repayment when the balance on the bank account is higher than the Protection Level. The Protection Level is set by the customer being an amount between £0 and £500. Where the customer has not pre-set a Protection Level, the default Protection Level will be set at £20 above the customer's overdraft limit.
- 2) Whenever IML takes an automatic repayment, it will leave the balance of the bank account at least £30 above the Protection Level to avoid triggering an auto borrowing drawdown of credit.
- 3) The automatic repayment amount will be the full amount owed by the customer in outstanding capital and interest.
- 4) The customer may cap each automatic repayment amount to a minimum of 25% of their credit limit or £100 (whichever is greater) and up to a maximum of the full balance outstanding. If a cap is set but the customer goes into arrears, IML may seek to take an amount up to the minimum monthly repayment plus arrears balance even if it exceeds the capped automatic repayment amount.
- 5) The minimum amount of money being paid into the customer's bank account which will trigger an automatic repayment to IML is £50. If the balance owed is less than £50, IML may take the full amount owed on a lesser amount being paid into the bank account.

4.13 Interest will be charged on the balance outstanding at a rate of 0.34% per day variable (equating to 25.5% per annum) for each day during which the customer has a balance outstanding whether for all or part of that day. Interest will be

charged on each drawdown of credit for a maximum of 75 days from the date of drawdown.

Identification of concerns

- 4.14 In February 2020, Supervision commenced a review of IML's creditworthiness practices. This review identified, amongst other issues, significant concerns around IML's method for testing customers' ability to repay and use of CPAs to collect repayments automatically. Supervision's findings and concerns cover both SafetyNet and Tappily.

Creditworthiness assessment

- 4.15 IML assumes a customer will repay the full capital balance plus interest over a reasonable period. In determining the reasonable period for a customer to repay, IML considers the typical time taken to repay a fixed sum unsecured personal loan for an amount equal to the credit limit. IML has determined the reasonable period for the customer to make repayment as three calendar months for SafetyNet, and four months for Tappily. IML also considers that customers can afford to apply up to 50% of their monthly net disposable income to making repayments.
- 4.16 IML's practice conflicts with information disclosed in its credit agreements, explanation documents and pre-contract credit information documents provided to customers. These documents indicate that IML has a contractual right, subject to relevant conditions, to take repayment of the full amount owed in outstanding capital and interest in one collection using a CPA when it sees a balance increase in the customer's bank account.
- 4.17 IML provided details of the time taken for balances on SafetyNet to be repaid to zero between 31 July 2019 to 30 June 2020. The analysis showed a high percentage of customers (between 5% and 42% depending on risk bands) repaid their balance to zero in less than a month. The analysis also showed that a lower proportion of customers (between 0% to 7% depending on the risk bands) repaid their balance to zero from month two to month six.
- 4.18 Supervision provided initial feedback to IML on 20 April 2021 noting that, based on a review of IML's product documentation and practice, IML appears to operate on the assumption it will collect the full capital balance plus interest when funds enter a customer's bank account. Supervision stated this assumption should be included within IML's creditworthiness assessment. Supervision explained that it did not consider repayment of the full amount owed in outstanding capital and interest based on equal monthly instalments to be a reasonable assumption for IML to make given the further assumption identified.
- 4.19 IML asserted that the practice of taking a repayment greater than the minimum monthly or Monthly Reasonable Repayment Amount (up to 50% of a customer's monthly net disposable income), complied with the Authority's rules because the fact a repayment up to the full capital balance plus interest may be taken is disclosed in the documentation provided to customers.
- 4.20 Supervision sent a second feedback letter to IML on 9 November 2021 stating that, in assessing creditworthiness and determining whether to include further reasonable assumptions, a firm should also consider the typical drawdown and repayment patterns of its customers. Supervision highlighted that IML's customers did not typically appear to make repayments in equal instalments over three months based on information on the time taken for balances on SafetyNet to be repaid to zero that IML provided. Supervision also noted that it did not appear to

be IML's intention to collect repayment over three months based on disclosures in the SafetyNet documentation provided to customers. Consequently, Supervision considered a further reasonable assumption based on repayment of the full capital balance plus interest should be included in IML's creditworthiness assessment.

4.21 IML responded insisting that applying a repayment assumption based on three months for SafetyNet is reasonable as this ensures in the majority of cases the assumed payments would not be made out of further borrowing, in contrast to applying an assumption based on collecting the full amount owed in capital and interest in one collection. IML also explained applying a repayment assumption based on one payment is not reasonable because a majority of its customers do not repay their full capital balance plus interest intra-month and are only contractually required to make the minimum monthly repayment to keep their account in good standing.

4.22 Supervision held a call and sent a third feedback letter to IML on 9 February 2022 reiterating its concern that IML is still not, after considering the individual circumstances of the customer and typical product use, making further reasonable assumptions about the timing, amount of drawdowns and repayments over the duration of the credit. Supervision stated that it remains of the view the assumption IML applies does not match its intended actions when collecting, potentially disadvantaging its customers.

4.23 IML replied with the following points:

- 1) IML assumes the customer will draw down the entire credit limit at the earliest opportunity and repay in equal instalments over three months for SafetyNet, which it considers to be a reasonable period. IML states this matches how the products are marketed and operate in practice. IML also states an equal instalment repayment model over 90 days or three months is prevalent in the credit market for competing loans of an equivalent amount.
- 2) IML explains that it does not make further assumptions by reference to a customer's individual circumstances because its products are accessed online, it does not meet the applicant to determine intended use or future cashflow requirements and the underwriting takes place on an automated basis. Consequently, IML does not have detailed information on the likely usage and expenditure patterns of each applicant. Together with the small sum consumer credit involved, IML considers it reasonable to apply a repayment assumption based on three equal monthly instalments for all SafetyNet customers, as opposed to particularising bespoke affordable assumptions for each customer. IML further states it does not consider the need to make further assumptions because it is always comfortable that its SafetyNet customers would repay the full debt in equal instalments over three months.
- 3) IML states it carries out weekly affordability checks on customers to identify changes in circumstances for an individual customer. Based on the outcomes of these weekly checks, it may reduce credit limits or bar further usage of the facility.
- 4) IML states it has increased the maximum value the SafetyNet Level and Tappily Protection Level can hold to £500, allowing customers to set a larger cash buffer from which no repayments will be taken. IML also highlights that customers no longer have to activate the Smart Top Up feature to adjust the SafetyNet Level and Tappily Protection Level as the setting of these levels have been decoupled from the automatic borrowing facility.

4.24 Supervision countered IML's response and reiterated its concerns through a fourth feedback letter on 6 June 2022:

- 1) Supervision notes that, even with the revised operation of the SafetyNet Level and Tappily Protection Level, it is unlikely a customer would repay the debt in equal monthly instalments. Supervision observes that upon signing a credit agreement, the customer provides consent to use of a CPA to collect up to the full amount owed in outstanding capital and interest at the initial collection attempt. Supervision considers this practice leads to an expectation that the debt would be repaid in a shorter period.
- 2) Supervision did not accept IML's explanation for making no further repayment assumptions by reference to a customer's individual circumstances. Supervision notes that IML has access to detailed information relating to an applicant's salary, for example, through open banking data at the point of lending. Supervision considers that IML could reasonably assume a repayment of up to the full capital balance plus interest would be collected when subsequent funds are made to the customer's bank account.
- 3) Supervision highlighted IML had previously indicated that SafetyNet and Tappily are two innovative and relatively complicated products which operate in a materially different way to other consumer credit products. Despite this acknowledgement, Supervision notes that IML is not considering the materially different way the products operate or the typical behaviour of the customers in using these products within its creditworthiness assessment.
- 4) In relation to the SafetyNet Level and Tappily Protection Level, Supervision highlighted the default values for these products remain unaltered and the operational changes made would unlikely be a sufficient mitigant because IML places responsibility on the customer to take steps to ensure repayments are and remain affordable, instead of assessing the customer's ability to repay the full amount owed in outstanding capital and interest. Supervision also expressed concerns over whether IML had communicated clearly to customers that a SafetyNet Level or Tappily Protection Level of £500 can be set independent of activating the Smart Top Up feature.
- 5) Supervision also referred to information relating to the time taken for balances on SafetyNet and Tappily to be repaid to zero provided by IML. On SafetyNet, Supervision observed that customers appear to be using the product for longer term borrowing and not as intended as the analysis showed a significant proportion of customers had never repaid either their outstanding balance at the start of the period to £0, or funds borrowed within that period to £0. For Tappily, Supervision noted that customers appear to be repaying the debt at a rate greater than assessed as affordable as the analysis showed the greatest proportion of customers were those who repaid their balance to zero intra-month.

Use of CPA

4.25 SafetyNet and Tappily use open banking data to monitor a customer's bank account and a CPA to collect repayments automatically. As part of the terms and conditions when applying for these products, the customer authorises IML to access their transaction data and bank balance under the open banking regime. This enables IML to provide its services, including periodically reviewing and monitoring the customer's bank account balance and to make lending and collection decisions.

4.26 When a customer enters the credit agreement, they must provide IML with a CPA

to collect repayments automatically from their nominated bank account. Subject to relevant conditions, including when £50 has been paid into the customer's bank account, IML will take an automatic repayment up to the full capital balance plus interest using the CPA. Should insufficient funds be available to collect the full amount owed in outstanding capital and interest, IML will instead seek to take the minimum monthly repayment on the date the customer's salary or other regular income is next anticipated to be paid into their bank account.

- 4.27 As part of Supervision's review, IML provided a sample of customer files. Within the sample reviewed, Supervision saw IML collecting sums intra-month via a CPA which collectively exceeded the monthly disposable income calculated as available for the customer. In many instances where an automatic repayment was collected within the month, the total sum collected via a CPA exceeded the Monthly Reasonable Repayment Amount assessed by IML as being affordable for the customer. Supervision became concerned that such collections practices left the customers with insufficient funds for non-discretionary expenditure and/or caused payments to be made from further borrowing.
- 4.28 Supervision wrote to IML on 20 April 2021 raising initial concerns with its use of CPAs. Supervision warned that IML would breach the Authority's rules should it request a payment service provider to take a payment from a customer's bank account where it had reason to believe there are insufficient funds in the account, or that taking the payment would leave insufficient funds to meet priority debts or other essential living expenses. Supervision noted that IML only tested a customer's ability to repay in equal monthly instalments rather than the full capital balance plus interest in one collection using a CPA. Supervision also noted that customers can set a SafetyNet Level which sits in their overdraft. Supervision expressed concern that the collection of unaffordable repayments could lead to insufficient funds being available. Supervision asked IML to clarify how it ensures a customer would be left with sufficient funds when seeking payments greater than the minimum monthly amount it had assessed as affordable for the customer.
- 4.29 IML responded to Supervision stating it was entirely satisfied the use of a CPA to take a sum greater than the reasonable assumed amount complied with the Authority's rules because:
- 1) The fact the full amount owed in outstanding capital and interest may be taken is disclosed in the customer journey, its website, the credit agreements and adequate explanation documents.
 - 2) The customer is left with a pre-agreed buffer of cash in their bank account when any repayment is taken.
 - 3) Any customers unhappy with a repayment taken by a CPA can request a full refund.
 - 4) IML would not attempt a CPA repayment if the customer is seen from their bank transactions to be experiencing financial difficulties or has disclosed this to IML.
- 4.30 Supervision sent a second feedback letter to IML on 9 November 2021. While recognising that IML left the customer with a pre-agreed buffer of cash when any repayment is taken, Supervision highlighted that if the levels are not set sufficiently high then the customer remains at risk of being left with insufficient funds, and the repayment could be made out of further borrowing if it takes the account overdrawn. Supervision stated that IML should only be using a CPA where it is satisfied there are sufficient funds for non-discretionary expenditure rather than

simply suspending its use when there are signs of financial difficulty or refunding payments upon the customer's request.

- 4.31 IML responded stating that SafetyNet and Tappily would cease to operate in the manner intended without use of CPAs. IML stated it would monitor that the use of CPAs is treating customers fairly. In response to Supervision's concern that repayments may take a customer's account overdrawn, IML indicated that if an applicant is already borrowing using their overdraft facility at the time of application, then it is likely they may continue to use their overdraft facility while using SafetyNet and Tappily.
- 4.32 Supervision held a call and sent a third feedback letter to IML on 9 February 2022 reiterating that IML's use of CPAs together with its practice of collecting up to the full capital balance plus interest may leave customers with insufficient funds. Supervision notes the SafetyNet Level and Tappily Protection Level hold default values of only £20 above their overdraft limit, and at least £30 above the SafetyNet Level and Tappily Protection Level will be left after a repayment. Supervision notes IML places the onus on the customer to make any adjustment to the SafetyNet Level and Tappily Protection Level so this feature appears to facilitate further lending rather than ensuring repayments remain sustainable. Supervision also expressed concern that IML appears to acknowledge that repayments may come from additional borrowing by taking an account overdrawn.
- 4.33 IML responded to the Authority with the following points:
- 1) IML states an automatic repayment does not invalidate its initial assumptions, result in customer disadvantage, or leave customers with insufficient funds. It states the system contains protections to ensure it does not take more than the customer can afford. IML highlights that a Tappily customer can set a repayment cap of at least 25% of their credit limit, which limits the repayments that can be taken by a CPA to this capped amount.
 - 2) IML has changed the way it uses CPAs for customers where its connection to open banking data is lost. Going forward, IML will limit its CPA use to one collection attempt of the contractual repayment amount.
 - 3) IML acknowledged that any repayment taken out of a bank account will increase the risk of there being insufficient funds for priority debts or other essential living expenses. IML argued that should it cease taking repayments out of an overdraft, this would risk potential detriment to the customer who might miss their contractual repayment amount and default as a result at a time where they have available funds to meet the repayment.
 - 4) As to Supervision's concern regarding the SafetyNet Level and Tappily Protection Level, IML stated it had undertaken a communications exercise to draw attention to this feature and the increased limit of £500 that can be set.
- 4.34 Supervision responded to IML and reiterated its concerns through a fourth feedback letter on 6 June 2022:
- 1) In relation to IML's assertion that the system contains protections to ensure that automatic repayments do not take more money than the customer can afford, Supervision highlighted that it has not seen evidence of meaningful and effective protections. With reference to the SafetyNet Level and Tappily Protection Level, Supervision notes the onus is placed on the customer to adjust the levels, otherwise a default value of £20 above the overdraft limit is applied. With at least £30 remaining in the balance after an automatic

repayment, this may take a customer within £50 of their overdraft limit. Supervision indicated that it does not consider these system protections to be sufficient when IML is collecting repayment for amounts greater than it has assessed as affordable.

- 2) While IML proposes limits to its use of CPAs where open banking connection has expired or been withdrawn, Supervision considers this will only benefit those customers while it is unlikely that other customers will proactively withdraw their open banking connection to benefit from this amendment. This approach also conflicts with disclosures in the credit agreements which state IML will attempt to take repayment for the full amount owed in outstanding capital and interest where it does not have access to real time banking data. Supervision also stated it is not aware of any communications by IML to articulate its change in approach.

Impact on customers

4.35 Separately, the Authority has undertaken Transaction Analysis on data provided by IML for SafetyNet to examine the borrowing pattern of customers, the interest incurred by the customers and the potential impact of IML's use of CPAs. The review covered:

- 1) Tranche 1 data relating to 20,834 accounts, £94,783 lent and £13,550,945 interest charges from 1 December 2019 to 1 February 2021; and
- 2) Tranche 2 data relating to 6,251 accounts, £16,108,091 lent and £1,946,586 interest charges from 12 May 2022 to 16 June 2022.

4.36 The Transaction Analysis observed the following practices:

- 1) A customer's account could repay and then borrow the full principal balance in a short period of time, known as a 'reset event'. The Transaction Analysis found that single day reset events are common and can occur multiple times for a significant portion of SafetyNet's customers. It observed 62.8% of all accounts had at least one single day reset event following a repayment, with 24% of accounts experiencing five or more reset events and 75.7% of accounts (across both tranches of data) experiencing at least one intra-week reset event.
- 2) A significant proportion of SafetyNet customers use the product persistently, with over 80% of accounts having an active debt for 75% of the time. Of the persistent users, c.50% borrowed sums which collectively exceeded seven times their average balance, indicating a high level of debt is being reset.
- 3) Borrowing reset events is a primary reason for continued interest charges in accounts where there is a stable outstanding balance. Each reset event 'renews' the debt, therefore, restarting the 40-day window in which interest will be charged by IML on SafetyNet. The Transaction Analysis found that for Tranche 1 data, on 70.1% of the accounts (where there was some level of debt outstanding for more than 75% of the time), the interest charged on the average balance exceeded 40 days. For Tranche 2 data, on 69.2% of the accounts (where there was some level of debt outstanding for more than 75% of the time), the interest charged on the average balance exceeded 40 days.
- 4) A prevalence of customers being taken overdrawn. The Transaction Analysis found that 26% of accounts in Tranche 1 and 22% of accounts in Tranche 2 are taken overdrawn by CPA collections, and that 38.5% of accounts in

Tranche 1 and 33.4% of accounts in Tranche 2 had CPA collections taken from the customers' overdraft.

- 4.37 The Transaction Analysis found that SafetyNet can be very costly if repayments via CPA collections are unsustainable, and the customer has to draw down again.

5 CONCLUSION

- 5.1 The regulatory provisions relevant to this Further First Supervisory Notice are set out in the Annex.

Analysis of failings and risks

Regulatory requirements

- 5.2 Based on the facts and matters described, IML may be operating in breach of Principle 6 (Customers' interests).
- 1) When conducting its creditworthiness assessment, IML assumes a customer will repay the full capital balance plus interest in equal instalments over three months for SafetyNet and four months for Tappily, up to 50% of a customer's monthly net disposable income. In practice, IML has a contractual right to collect sums greater than the minimum monthly or Monthly Reasonable Repayment Amount it has assessed the customer can afford, including in one collection. This is in potential breach of CONC 5.2A.27R(1).
 - 2) At the point of lending, IML has access to detailed open banking data relating to the applicant and could therefore make further reasonable assumptions to inform its assessment of the customer's ability to repay. Rather than applying an assumption that considers the customer's individual circumstances, IML relies on an initial repayment assumption which is unlikely to match the product usage. IML is also not considering the materially different way the products operate, or the typical behaviour of customers using its product. This is in potential breach of CONC 5.2A.27R(3), and not following the guidance of CONC 5.2A.28G.
 - 3) IML monitors a customer's bank account and uses a CPA to collect repayments automatically of up to the full amount owed in outstanding capital and interest when relevant conditions are met. The Authority is concerned that this practice may leave the customer with insufficient funds to meet priority debts or other essential living expenses. Although IML states that protections are built into its systems, they are not sufficient since they place the onus on the customer to take adequate steps. This is a potential breach of CONC 7.6.3R, and does not follow the guidance in CONC 7.6.5G(2).
 - 4) IML's use of a CPA and taking repayment of the full capital balance plus interest in one collection attempt may also lead the customer to borrow further from IML or another firm, or to enter their overdraft facility to meet such expenses. IML acknowledges that automatic repayments may take a customer's account overdrawn but has not changed its practice to prevent this occurring. This is a potential breach of CONC 5.2A.12R.
- 5.3 The facts and matters taken together casts serious doubts that IML is treating customers fairly.

The Authority's consumer protection objective

- 5.4 The Authority's operational objective of consumer protection requires the Authority to ensure an appropriate degree of protection for consumers (section 1C(1) of the Act).
- 5.5 Upon signing a credit agreement for SafetyNet or Tappily, the customer provides consent for IML to use a CPA to collect sums up to the full amount owed in outstanding capital and interest from the initial collection attempt. The terms of the credit agreements, along with the operation of the CPA, lead to an expectation the debt will be repaid in a shorter period.
- 5.6 Affordability risks to borrowers are likely to depend both upon the nature and risks of the credit product, and the characteristics of the customer and their likely ability to repay. Where risks are higher, a more rigorous assessment is likely to be needed. Rather than applying an assumption that considers the customer's individual circumstances, IML relies on a repayment assumption that is unlikely to match the product usage. IML's practice is not reasonable and may cause the customer to repay debt at a rate greater than they can afford and risks placing them in financial difficulty.
- 5.7 The Authority has concluded, in light of the facts and matters set out, that it is appropriate to exercise its own-initiative power under section 55L(2) and (3) of the Act by imposing the Requirements on IML.
- 5.8 The Authority considers that the Requirements are a proportionate means to address the current and immediate risks, and are desirable in order to advance the Authority's operational objective of consumer protection.

Timing and duration of the Requirements

- 5.9 It is necessary to impose the Requirements on an immediate basis given the seriousness of the risks and the need to protect consumers in accordance with EG 8.3.3(1) which provides the Authority may impose a requirement so that it takes effect immediately as IML has not taken substantive steps to address the Authority's fundamental concerns such that there a risk of loss, or other adverse effect on consumers and the need to protect consumers' interests.
- 5.10 The Authority considers that it is necessary for the Requirements to remain in place until such time as the Authority is satisfied they can be lifted.

6 PROCEDURAL MATTERS

Decision-maker

- 6.1 The decision which gave rise to the obligation to give this Further First Supervisory Notice was made by an Authority staff member under executive procedures according to DEPP 2.3.7G and DEPP 4.1.7G.
- 6.2 This Further First Supervisory Notice is given under section 55Y(4) and in accordance with section 55Y(5) of the Act.
- 6.3 The following statutory rights are important.

Representations

- 6.4 IML has the right to make written representations to the Authority (whether or not

it refers this matter to the Tribunal). IML may also request to make oral representations but the Authority will only consider this in exceptional circumstances according to DEPP 2.3.1AG. The deadline for providing written representations and notifying the Authority that IML wishes to make oral representations is 3 January 2023 or such later date as may be permitted by the Authority. Any notification or representations should be sent to the SPC Decision Making Secretariat (SPCDecisionMakingSecretariat@fca.org.uk).

The Tribunal

- 6.5 IML has the right to refer the matter to which this Further First Supervisory Notice relates to the Tribunal. The Tax and Chancery Chamber is part of the Tribunal which, amongst other things, hears references arising from decisions of the Authority. Under paragraph 2(2) of Schedule 3 of the Tribunal Procedure (Upper Tribunal) Rules 2008, IML has 28 days from the date on which this Further First Supervisory Notice is given to it by 17 January 2023 to refer the matter to the Tribunal.
- 6.6 A reference to the Tribunal can be made by way of a reference notice (Form FTC3) signed by or on behalf of IML and filed with a copy of this Further First Supervisory Notice. The Tribunal's contact details are: The Upper Tribunal, Tax and Chancery Chamber, 5th Floor, Rolls Building, Fetter Lane, London EC4A 1NL (telephone: 020 7612 9730; email: uttc@hmcts.gsi.gov.uk).
- 6.7 Further information on the Tribunal, including guidance and the relevant forms to complete, can be found on the HM Courts and Tribunal Service website: <http://www.justice.gov.uk/forms/hmcts/tax-and-chancery-upper-tribunal>
- 6.8 IML should note that a copy of the reference notice (Form FTC3) must also be sent to the Authority at the same time as a reference is filed with the Tribunal. A copy of the reference notice should be sent to the SPC Decision Making Secretariat (SPCDecisionMakingSecretariat@fca.org.uk).

Confidentiality and publicity

- 6.9 IML should note that this Further First Supervisory Notice may contain confidential information and should not be disclosed to a third party (except for the purpose of obtaining legal advice on its contents).
- 6.10 IML should note that section 391(5) of the Act requires the Authority, when the Further First Supervisory Notice takes effect, to publish such information about the matter to which the notice relates as it considers appropriate.

Authority contacts

- 6.11 Any questions regarding the executive procedures decision-making process should be directed to the SPC Decision Making Secretariat (SPCDecisionMakingSecretariat@fca.org.uk).

Decision made under Executive Procedures Head of Department

Annex

RELEVANT STATUTORY PROVISIONS

1. The Authority's operational objectives established in section 1B of the Act include securing an appropriate degree of protection for consumers (section 1C).
2. Section 55L of the Act allows the Authority to impose a new requirement on an authorised person if it appears to the Authority that the authorised person is failing, or likely to fail to satisfy the Threshold Conditions (section 55L(2)(a)), or it is desirable to exercise the power in order to advance one or more of the Authority's operational objectives (section 55L(2)(c)). This power is referred to as the Authority's own initiative requirement power.
3. Section 55N of the Act allows a requirement to be imposed under section 55L of the Act so as to require the person concerned to take specified action (section 55N(1)(a)), or to refrain from taking specified action (section 55N(1)(b)). Section 55N(2) provides that a requirement may extend to activities which are not regulated activities.
4. Section 55Y(3) of the Act allows a requirement imposed under the own initiative requirement power to take effect immediately (or on a specified date) only if the Authority, having regard to the ground on which it is exercising its own initiative power, reasonably considers that it is necessary for the requirement to take effect immediately (or on that date). Section 55Y(4) of the Act provides that if the Authority proposes to vary a Part 4A permission, or to impose or vary a requirement, or varies a Part 4A permission or varies a requirement, with immediate effect, it must give the authorised person written notice. Section 55Y(5) of the Act states that the notice must: (a) give details of the variation of the permission or the requirement or its variation; (b) state the Authority's reasons for the variation of permission or the imposition or variation of the requirement; (c) inform the authorised person that it may make representations to the regulator within such period as may be specified in the notice; (d) inform the authorised person of when the variation of the permission or the imposition or variation of the requirement takes effect; and (e) inform the authorised person of its right to refer the matter to the Tribunal.
5. Section 391 of the Act provides that:
“[...]”
 - (5) When a supervisory notice takes effect, the Authority must publish such information about the matter to which the notice relates as it considers appropriate.
 - (6) But the Authority may not publish information under this section if in its opinion, publication of the information would, be unfair to the person with respect to whom the action was taken or proposed to be taken [or] prejudicial to the interests of consumers or detrimental to the stability of the UK financial system.
 - (7) Information is to be published under this section in such manner as the Authority considers appropriate.”

RELEVANT REGULATORY PROVISIONS

The Principles for Businesses

6. The Principles for Businesses (PRIN) are a general statement of the fundamental obligations of firms under the regulatory system. PRIN 1.1.2R provides that they

derive their authority from the Authority's rule making powers as set out in the Act and reflect the statutory objectives. The Principles are set out at PRIN 2.2.1.

7. Principle 6 (Customers' interests) provides that a firm must pay due regard to the interests of its customers and treat them fairly.

Consumer Credit sourcebook

8. The section of the Handbook entitled Consumer Credit sourcebook (CONC) sets out the detailed obligations that are specific to credit related regulated activities and activities connected to those activities carried on by firms.

9. CONC 5.2A.12R states that the firm must consider the customer's ability to make repayments under the agreement:

[...]

- (3) without the customer having to borrow to meet the repayments;
 - (4) without failing to make any other payment the customer has a contractual or statutory obligation to make; and
 - (5) without the repayments having a significant adverse impact on the customer's financial situation.
10. CONC 5.2A.27R(1) states that in relation to entering into a regulated credit agreement for running account credit, the firm must ensure that the customer draws down the entire credit limit at the earliest opportunity and repays by equal instalments over a reasonable period.
 11. CONC 5.2A.27R(3) states that, if, after considering the individual circumstance of the particular customer of which the firm is aware at the time the creditworthiness assessment is carried out, it is reasonable to make further assumptions about the timing and amounts of drawdowns of credit and repayments over the duration or likely duration of the credit, then the firm must do so and these assumptions must be reasonable ones.
 12. CONC 5.2A.28G indicates that:
 - (1) Unless (2) applies, the firm should, when making an assumption about the length of a reasonable period for repayment for the purposes of CONC 5.2A.27R(1) or (2), have regard to the typical time required for repayment that would apply to a fixed-sum unsecured personal loan for an amount equal to the credit limit. The firm should take into account the terms and conditions of a loan likely to be available to that customer (whether from the firm or from another lender) and any other factors that the firm reasonably considers to be relevant.
 - (2) If, however, after considering the individual circumstances of the particular customer of which the firm is aware, it is reasonable to make a different assumption about the length of a reasonable period for repayment, the firm may do so. This may be the case, for example, where the level of the periodic minimum repayment due under the terms of the agreement is such that, if the customer complied with those terms, the drawdown of the credit limit would be repaid more quickly than the typical duration of a fixed-sum loan for an equivalent amount.
 - (3) This sub-paragraph applies if it is reasonable to make further assumptions for the purposes of CONC 5.2A.27R(3), in addition to the assumptions described

in CONC 5.2A.27R(1) or (2). In those circumstances, the firm should, when deciding what a reasonable assumption is, have regard to typical drawdown and repayment patterns of its customers in relation to that product or type of product, or of customers of that type generally, but should also consider any factors particular to the individual customer, where known. It may or may not be reasonable to make further assumptions in respect of the initial reasonable period referred to in CONC 5.2A.27R(1) or (2), as well as in respect of the subsequent duration of the credit, depending on those factors.

13. CONC 7.6.3R states a firm must exercise its rights under a continuous payment authority in a manner which is reasonable, proportionate and not excessive and must exercise appropriate forbearance if it becomes aware that the customer is or may be experiencing financial difficulties.
14. CONC 7.6.5G(2) indicates that a firm is likely to contravene CONC 7.6.3R if it requests a payment service provider to make a payment from the customer's payment account where it has reason to believe that there are insufficient funds in the account or that taking the payment would leave insufficient funds for priority debts or other essential living expenses (such as in relation to a mortgage, rent, council tax, food bills or utility bills)

The Enforcement Guide

15. The Authority's approach in relation to its enforcement powers is set out in Chapter 8 of the Enforcement Guide (EG), certain provisions of which are summarised below.
16. EG 8.1.1 reflects the provisions of section 55L of the Act by stating that the Authority may use its own-initiative power to impose requirements on an authorised person where, amongst other factors, the person is failing or is likely to fail to satisfy the threshold conditions for which the Authority is responsible (EG 8.1.1(1)), or it is desirable to exercise the power in order to advance one or more of its operational objectives (EG 8.1.1(3)).
17. EG 8.2.1 states that when the Authority considers how it should deal with a concern about a firm, it will have regard to its statutory objectives and the range of regulatory tools that are available to it. It will also have regard to the principle that a restriction imposed on a firm should be proportionate to the objectives the Authority is seeking to achieve (EG 8.2.1(2)).
18. EG 8.2.3 states that in the course of its supervision and monitoring of a firm or as part of an enforcement action, the Authority may make it clear that it expects the firm to take certain steps to meet regulatory requirements. In the vast majority of cases the Authority will seek to agree with a firm those steps the firm must take to address the Authority's concerns. However, where the Authority considers it appropriate to do so, it will exercise its formal powers under section 55L of the Act to impose a requirement to ensure such requirements are met. This may include where, amongst other factors, the Authority has serious concerns about a firm, or about the way its business is being or has been conducted (EG 8.2.3(1)), or is concerned that the consequences of a firm not taking the desired steps may be serious (EG 8.2.3(2)).
19. EG 8.3.1 states that the Authority may impose a requirement so that it takes effect immediately or on a specified date if it reasonably considers it necessary for the requirement to take effect immediately (or on the date specified), having regard to the ground on which it is exercising its own-initiative powers.

20. EG 8.3.2 states that the Authority will consider exercising its own-initiative power as a matter of urgency where: 1) the information available to it indicates serious concerns about the firm or its business that need to be addressed immediately; and 2) circumstances indicate that it is appropriate to use statutory powers immediately to require and/or prohibit certain actions by the firm in order to ensure the firm addresses these concerns.
21. EG 8.3.3 states that it is not possible to provide an exhaustive list of the situations that will give rise to such serious concerns, but they are likely to include one or more of four listed characteristics, these include: 1) information indicating significant loss, risk of loss or other adverse effects for consumers, where action is necessary to protect their interests; 2) information indicating that a firm's conduct has put it at risk of being used for the purposes of financial crime, or of being otherwise involved in crime; 3) evidence that the firm has submitted to the Authority inaccurate or misleading information so that the Authority becomes seriously concerned about the firm's ability to meet its regulatory obligations; 4) circumstances suggesting a serious problem within a firm or with a firm's controllers that calls into question the firm's ability to continue to meet the threshold conditions.
22. EG 8.3.4 states that the Authority will consider the full circumstances of each case when it decides whether an imposition of a requirement is appropriate and sets out a non-exhaustive list of factors the Authority may consider, these include the extent of any loss, or risk of loss, or other adverse effect on consumers (EG 8.3.4(1)).
23. EG 8.3.4(9) includes the impact that use of the Authority's own-initiative powers will have on the firm's business and on its customers. The Authority will need to be satisfied that the impact of any use of the own-initiative power is likely to be proportionate to the concerns being addressed, in the context of the overall aim of achieving its statutory objectives.