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The Consumer Credit Bill

Bill 16 of 2004-05

Announced in the Queen's Speech on 23 November 2004, the *Consumer Credit Bill* was introduced into the House of Commons on 16 December 2004. It is due to be debated on Second Reading on 13 January 2004. Explanatory Notes to the Bill have also been published [Bill 16-EN].

The Bill follows the publication in December 2003 of a Government White Paper, "Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century" and a three-year review on modernising the UK's consumer credit laws. The Bill principally amends the *Consumer Credit Act 1974*. It seeks to enhance consumer rights and redress by replacing the 'extortionate' credit provisions with a new 'unfair credit relationship' test and introducing an Alternative Dispute Resolution scheme to be run by the Financial Ombudsman Service. It also seeks to strengthen the credit licensing system and equip the Office of Fair Trading with new powers to take action against rogue lenders. Finally, it seeks to extend regulation to all consumer credit and hire transactions (with limited exceptions).

This Paper provides a summary of the background to, and the main provisions of, the Bill.

Lorraine Conway

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Summary of main points

The *Consumer Credit Act 1974* (the 'CCA 1974') is the main Act designed to regulate consumer credit in the UK. The Government has long recognised that the CCA 1974 is in need of reform. The CCA 1974 is criticised for not providing sufficient protection for consumers, restricting rights of redress, and for failing to provide regulators with sufficient powers to tackle improper or unfair conduct by businesses in a burgeoning consumer credit industry.

In December 2003, the Department of Trade and Industry (DTI) published a White Paper, '*Fair, Clear and Competitive – the Consumer Credit market in the 21st Century*'. This followed a three-year review of the UK's consumer credit laws characterised by extensive consultations. In June and October 2004, new Regulations were made, which reform the requirements for pre-contractual conduct and disclosure by consumer credit businesses and the rules in relation to early settlement. In July 2004, the DTI, with the Department for Work and Pensions, published an Action Plan for tackling the problem of over-indebtedness. On 16 December 2004, the *Consumer Credit Bill* had its First Reading in the House of Commons. The aims of the Bill which seeks to reform (not replace) the CCA 1974 are:

- To enhance consumer rights and redress - by replacing the current 'extortionate credit' test with a new test based on unfairness, and by introducing an Alternative Dispute Resolution (ADR) scheme to be run by the Financial Ombudsman Service.
- To strengthen the regulation of consumer credit businesses - by creating a more targeted credit licensing regime and equipping the Office of Fair Trading (OFT) with new powers (by way of intermediate sanctions) to take action against rogue traders, including financial penalties.
- To extend regulation to all types of consumer credit and hire agreements (subject to limited exemptions) – by abolishing the financial limit that currently restricts protection under the CCA 1974 to loans of £25,000 or less.
- To provide debtors with new post-contractual information.

Commenting on the aims of the Bill in its Regulatory Impact Assessment, the DTI said:

The proposed reforms are not intended to affect any particular sector of the consumer credit market more than any other. [...] The reforms are intended to ensure that all consumer credit businesses act according to consistent rules and standards of conduct in the operation of their businesses and in relation to the provision of credit to consumers.

The Bill applies to the whole of the UK. Consumer credit is a devolved matter for Northern Ireland but as the Northern Ireland Assembly is currently suspended, Ministers have agreed that the Bill should extend to Northern Ireland.

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I Outline of current provisions of the CCA 1974

1. Regulated credit agreements

The consumer credit industry is substantial and diverse. Consumer credit businesses can include banks, home credit companies, mail order companies, those providing credit for goods, credit cards, store cards, debt collectors, financial advisers and credit brokers. According to the OFT, the consumer credit market is characterized “by strong competition – the UK consumer credit market is often cited as the most developed in Europe and no single firm has more than a 10% share of the market”.¹

The CCA 1974 established the current structure of regulation governing the provision of consumer credit or the supply of goods on hire or hire purchase to ‘individuals’ in the UK.² For the purposes of the CCA 1974, ‘individuals’ includes natural persons, unincorporated associations and partnerships of any size where the credit provided or payments for hire do not exceed a specified limit (currently £25,000).³ The CCA 1974 does not apply to credit or hire agreements made between traders and corporate bodies such as limited companies. The main objective of the CCA 1974 is “to provide for the small individual borrower the protection he unquestionably needs without setting up artificial barriers between one sort of credit and another.”⁴

There are many types of agreement which can come within the terms of a ‘regulated consumer credit agreement’ (provided they do not exceed the financial limit of £25,000). These include:

- hire purchase
- conditional sale
- credit sale
- personal loan
- overdraft
- loan secured by way of a second charge (land mortgage)
- credit card
- pledges
- budget accounts in shops

The CCA 1974 contains detailed rules covering:

¹ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004, p.19

² The CCA 1974 currently applies to the whole of the UK – with certain special provisions for Northern Ireland, which do not affect the substance of the statutory regime

³ When first introduced, the CCA 1974 covered most credit agreements up to a financial limit of £5,000, this was increased to £15,000 in 1985, and increased again in 1998 to its present limit of £25,000 – each increase was to reflect inflation

⁴ *Consumer Credit*, Cmnd 4596, Report of the Committee, Lord Crowther, 1971, (s) 6.6.3 – 6.64

- the form and content of agreements;
- the advertising of credit;
- the method of calculating the Annual Percentage Rate [APR] of the total charge for credit;
- the procedures to be adopted in the event of default, termination, or early settlement;
- extortionate credit bargains;
- individuals' access to credit reference files;
- equal liability of creditors and suppliers for misrepresentation or breach of contract by the latter; and
- hire purchase transactions.

In effect, the CCA 1974 regulates all aspects of individual consumer credit or consumer hire agreements including: entry into agreements (Part 5), matters arising during the currency of the agreement (part 6); and default under and the termination of agreements generally (part 7). The CCA 1974 also regulates the giving of security in relation to the agreements it regulates and pawn-broking (part 8) and the licensing of ancillary credit business (part 10).

In certain limited circumstances, a consumer credit or consumer hire agreement can be taken outside the control of the CCA 1974 by one of the limited exemptions listed in section 16 of the Act and in the *Consumer Credit (Exempt Agreements) Order 1989* (as amended).

2. Scope of the CCA 1974

The CCA 1974 is large: it is made up of twelve parts and supplemented by a mass of regulations, orders and notices. Consequently, it is not possible to summarise the full scope of the CCA 1974 within one Paper. However, the following examples illustrate how the CCA 1974, through its licensing regime and other targeted regulations, seeks to protect consumers:

- for credit agreements signed away from trade premises, following face-to-face discussions, the Act gives consumers a 'cooling-off' period, allowing the borrower to cancel the credit agreement within a certain period of time;
- a creditor cannot demand early payment, try to get the goods back, or end the agreement without first serving a written notice, 7 days before taking action;
- if the borrower has paid a third of the total price of the goods under a HP agreement, then the creditor cannot take the goods back without first getting a court order;
- if a credit agreement is 'extortionate', then the borrower can on application, ask the court to look at the agreement (see below);
- in a case where the seller of the goods and the provider of credit are not the same, the borrower can make a claim against either party in the event of non-performance of

the contract (e.g. in the case of a faulty good where the seller is no longer in business, the borrower can make a claim against the supplier of credit;

- certain written information must be provided to the borrower for the credit agreement to be enforceable, including the total cost of credit, the APR and the cash price for the goods.

3. Regulation of extortionate credit terms under the CCA 1974

Under current legislation there is no legal cap on the level of interest that can be charged on a consumer loan. It is not illegal for a lender to charge a high rate of interest. In determining the amount of APR to charge to a loan, the lender makes a commercial decision based on all the circumstances of the case. However, under sections 137-140 of the CCA 1974, a borrower can ask the court to re-examine a credit agreement if the rate of interest is extortionate.

The court's power to reopen a credit agreement can only be exercised:

- (a) on an application made by the debtor or anyone who has provided security for the credit agreement; or
- (b) at the request of the debtor or a surety in any proceedings to enforce the credit agreement, or other proceedings where the amount paid or payable under the agreement is relevant.

Under section 138(1) a credit bargain is deemed to be extortionate if it:

- (a) requires the debtor or a relative of his to make payments (whether unconditionally, or on certain contingencies) which are grossly exorbitant, or
- (b) otherwise grossly contravenes ordinary principles of fair trading.

In determining a case, the court is required to consider all the evidence before it including:

- prevailing interest rates at the time the bargain was made;
- the debtor's circumstances (e.g. age, experience, or the degree to which the debtor was under financial pressure at that time);
- the creditor's circumstances (e.g. the degree of accepted risk having regard to the value of any security).⁵

⁵ Sections 137-140 of the CCA 1974

Under section 139(2) of the CCA 1974, if the court concludes that the credit agreement is extortionate, then it may do a number of specified things “for the purpose of relieving the debtor or a surety from payment of any sum in excess of that fairly due and reasonable.” For example, the court may alter the terms of the agreement or require the creditor to repay sums already paid by the debtor.

4. Role of licensing

The CCA 1974 is underpinned by the Consumer Credit Licensing System, which is administered by the OFT.⁶ A licence is required for conducting business concerning the provision of credit, or the hiring of goods to the value of £25,000 or less, under a regulated agreement to an individual or non-corporate body.⁷ A licence is also required to carry out certain ancillary credit businesses. Currently, a consumer credit licence can cover any of the following six categories of trading:

- consumer credit
- consumer hire
- credit brokerage
- debt adjusting and debt counselling
- debt collecting
- credit reference agencies

It is quite legal for a business to be registered under more than one category, or to vary their licence in accordance with their business, while the licence is still in force.

Licences are granted to applicants who satisfy the OFT that they are ‘fit’ to carry on the type of business in question. In determining whether a person is fit to hold such a licence, the OFT must take into account all relevant circumstances and, in particular, any evidence that shows the applicant – or persons connected with that business – has been involved in any of four specific classes of activity:

- certain offences – involving fraud, dishonesty or violence;
- breach of the CCA 1974 or any other consumer protection legislation;
- discrimination; or
- business practices appearing to be deceitful, oppressive, unfair or otherwise improper – whether unlawful or not.

A licence is usually valid for five years after which time it must be renewed. However, the OFT can refuse, suspend or revoke a licence (subject to appeal). The overriding aim of the

⁶ The Office of Fair Trading exercises its responsibilities under the CCA 1974 across the whole of the UK: <http://www.oft.gov.uk/default.htm>

⁷ See page 7 of this Research Paper for statutory definition of ‘individual’

licensing regime is to ensure that, so far as possible, those operating in UK credit and hire markets have high standards of integrity.

II Failings of current legislation

Statistics on the growth and levels of consumer borrowing and the distribution of unsecured debt in the UK are set-out in a Library standard note, *Consumer Borrowing*, dated 7 January 2005.⁸ Information on levels of financial exclusion in the UK and the work of the Government's Social Exclusion Unit is also provided in a Library standard note, *Financial Exclusion*, dated 9 December 2004.⁹

A. Scale of the problem

Since the introduction of the CCA 1974, the UK credit market has been transformed. Before the financial deregulation of the 1980s building societies only provided mortgages, banks provided consumer loans and overdrafts and supermarkets sold fruit and vegetables. Now, the market for credit has become highly developed and diversified. The number of licensed lenders, the range and complexity of credit products and the sales strategies used by creditors has developed at an unprecedented rate. This blurring of the boundaries has undoubtedly increased competition but it may also have contributed to some of the less desirable aspects of market behaviour.

Not only have finance providers changed but their sales methods have too. Mailshots offering 'guaranteed' loans and credit approved after a few clicks on an internet site are now ubiquitous. In 1974 an application for a loan more likely meant an interview with a bank manager. Building societies regularly demanded that individuals saved with them for a number of years before they considered granting a mortgage. Now they battle over business with discounts and other inducements.

Given these developments it is not surprising that UK consumers avail themselves of the services of lenders much more now than in the past. The DTI estimates that the average level of outstanding debt per person, in real terms, has risen from £86 in 1969 to over £2,700 today. Thirty years ago, £32 million was owed on credit cards, now over £49 billion is owed.¹⁰

There is concern among consumer representative groups, including the National Association of Citizens Advice Bureaux (NACAB), about the level of debt in the UK and, in particular, about extortionate credit agreements.¹¹

⁸ Library standard note, *Consumer Borrowing*, SN/EP/2901, 7 January 2005

⁹ Library standard note, *Financial Exclusion*, SN/BT/3197, 9 December 2004

¹⁰ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

¹¹ National Association of Citizens Advice Bureaux, *Daylight robbery: the CAB case for effective regulation of extortionate credit*, December 2000

Citizens Advice (England and Wales) estimates that there has been a year-on-year increase in debt problems of 3.1% since 2003, whilst Citizens Advice Scotland estimates that there has been an increase in consumer credit enquiries over the past 4 years of approximately 3-5% per year.¹²

Statistics quoted by the DTI in its Regulatory Impact Assessment (RIA) of the Bill show that personal debt levels (excluding first and second charge mortgages) have increased significantly over the past five years, with approximately £170 billion outstanding as at July 2004 (compared to approximately £70 billion in 1993).¹³ The Finance & Leasing Association (FLA) estimates that its members lent a total of around £1.3 billion in direct unsecured loans to consumers.¹⁴

Consumer groups argue variously that there has been some exploitative conduct in the consumer credit market, to the detriment of the consumer.¹⁵ They argue that the complexity and lack of transparency of some financial products make it difficult for consumers to pick the right product for their needs, and that loans often tie people in for the long-term and include penalties for early repayment. There is also concern that some lenders are acting irresponsibly by failing to make sure consumers can afford the cost of credit.

A second distinct problem is that of financial exclusion. Whilst the vast majority of consumers have access to affordable and flexible credit, a significant number do not. This point was made in a recent Treasury report:

In recent decades, the majority of households have seen a dramatic rise in the availability, flexibility and affordability of credit. However, while the majority borrow using mainstream credit cards, bank loans and overdrafts at relatively low rates of interest, those on the lowest incomes often have to borrow to make ends meet, at interest rates many times that of a standard overdraft.¹⁶

The scale of the problem of financial exclusion was set out in a report published by a Treasury Policy Action Team in November 1999.¹⁷ It was estimated that about 1.5 million low income households use no financial services (representing over two million adults). Several reasons were given for this financial exclusion:

¹² Citizens Advice Annual Report 2003/2004, p.12

¹³ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004, p.4

¹⁴ The Finance and Leasing Association, Monthly Statistics, available at: http://www.fla.org.uk/fla_home/press_releases/070904.htm

¹⁵ HM Treasury, *Promoting financial inclusion*, December 2004

¹⁶ Ibid

¹⁷ HM Treasury website at: <http://www.hm-treasury.gov.uk/media/E0A85/pat14.pdf#page=69>

The reasons poor people use financial services less are complex. Outright refusal by banks or other institutions to do business with them is relatively rare. More often, the problem is mismatch between potential customers' needs and the products on offer. As providers develop new products that are more suitable for low income customers, those who live in poor neighbourhoods should benefit, as well as those in less deprived areas. Product diversity is clearly part of the answer, for all underserved markets.

People in poor neighbourhoods may make little use financial services for reasons that are related to the area itself. Where crime rates are high, property insurance, both household and business, may be unaffordable. Remoteness from major commercial centres, and the withdrawal of financial service outlets from poor communities, may be factors in low income households' non-use of mainstream institutions. The development of new delivery channels can overcome this factor. There is no single solution: again, diversity is of the essence.¹⁸

A more recent Treasury report divided the non-mainstream credit market into the 'non-status' and 'alternative' markets.¹⁹ Non-status lending principally involves the offer of credit products similar to those in the mainstream sector (such as personal loans and credit cards) to people with poor credit ratings who would normally find it difficult to obtain credit from traditional lending institutions. Whilst one would expect non-status loans to attract a higher rate of interest than an ordinary credit arrangement (to reflect the higher risk of default to the lender), some appear to charge punitively high rates or dual rates.²⁰ There is also concern that vulnerable borrowers may be inadequately informed about the terms of some loans.

The alternative credit market exists to meet the needs of low-income households requiring access to small, short-term loans, catering for people whose needs are not adequately met by mainstream credit providers. Commenting on the current state of the alternative credit sector, the Treasury report said:

Reliance on the alternative credit market means that the most vulnerable consumers typically end up paying much more for credit. Typical alternative credit products have Annual Percentage Rates (APRs) over 100 per cent – many times the APRs of standard mainstream personal loans, overdrafts and credit cards. For example:

- a typical loan from a home collected credit company for £200 might attract a charge of £94, which is repaid over 30 weeks (309 per cent APR) at £10 a week;²¹

¹⁸ Treasury Policy Action Team 14, *Financial Exclusion*, p 1, November 1999

¹⁹ HM Treasury, *Promoting financial inclusion*, December 2004

²⁰ In broad terms, a dual rate is where two interest rates are quoted in the agreement; the higher rate comes into force if the borrower defaults on the loan

²¹ *Access to credit on a low income: a study into how people on low incomes in Liverpool access and use consumer credit*, Paul A Jones, Co-operative Bank, 2001

- pawnbrokers charge interest each month for the length of the loan. A loan from a pawnbroker would have a monthly interest rate of around 7-12 per cent. A loan of £200 over 4 months, at 7 per cent interest a month would equate to a charge of £56 and an APR of 110 per cent;²² and
- an example from Citizens Advice Bureau in Merseyside highlights the costs of sale and buyback. One client received £45 from selling a television/video recorder that he had bought for £500, 12 months previously.²³ The item was recoverable by him paying £56.25 within 28 days, equivalent to an APR of 1355 per cent. Due to confusion over the date on the contract, the item was sold before the client could recover it, with the resale price being £120.²⁴

Treasury research data suggests that clients of the non-status or alternative credit markets are likely to be: people on low incomes, with a poor history of employment; the elderly; single parents; and those with a long-term illness or disability.²⁵ The DTI estimates that potentially some 9 million consumers now lack the credit rating needed to borrow mainstream products from high street lenders.²⁶

In its report *Unjust Credit Transactions*, the OFT concluded that the extortionate credit provisions of the CCA 1974 were insufficient to protect consumers, particularly those with an impaired or low credit rating who have limited sources of finance available to them.²⁷ Similarly, in its 2001 report, *Daylight Robbery*, the NACAB argued:

... the solution to the problem of extortionate credit lies in effective legislation that is accessible to the consumer and improving the ability of consumers to make informed choices from a range of credit options.²⁸

The Government 2003 White Paper, *Fair, Clear and Competitive – the Consumer Credit Market in the 21st Century*, refers to research commissioned by the DTI into the impact on consumers of exploitative conduct by some businesses in consumer credit transactions: conduct which is either unfair or in breach of general standards of good conduct. The DTI has also reviewed evidence of the number and nature of enquiries made by consumers to

²² *Pawnbrokers and their customers*, Sharon Collard and Elaine Kempson, The Personal Finance Research Centre, University of Bristol, October 2003

²³ National Association of Citizens Advice Bureaux, *Daylight Robbery - The CAB case for effective regulation of extortionate credit*, December 2000

²⁴ HM Treasury, *Promoting financial inclusion*, December 2004

²⁵ Office of Fair Trading, *Left out in the cold*, 22 April 1999

²⁶ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004, p.4

²⁷ Office of Fair Trading, *Unjust Credit Transactions*, September 1991

²⁸ The National Association of Citizens Advice Bureaux, *Daylight Robbery – The CAB case for effective regulation of extortionate credit*, December 2000

government bodies and advice providers (such as Citizens Advice). On the basis of this information, the DTI has identified the following trends:

- the number of consumer enquiries to free advice services about consumer credit is increasing; and
- the total value of the credit that is the subject of these enquiries is increasing.

However, the difficulty of accurately quantifying consumer detriment is readily acknowledged by the DTI:

While we cannot accurately quantify its full extent, it is considerable, and based on recent trends, increasing. A failure to reform the Act to allow for more effective consumer redress will allow the current situation to continue and potentially worsen.²⁹

In the RIA of the new *Consumer Credit Bill*, the DTI identified the four main causes of consumer detriment, which it suggests may often be combined in a single enquiry:

(a) unfairness in respect of any aspect of the consumer credit relationship, and most particularly in relation to:

- (i) the use of misleading and unfair selling methods, including irresponsible lending;
- (ii) the administration of the agreement (including the abuse of a lender's discretionary powers to vary terms or the manner in which they operate);
- (iii) unfair treatment of accounts in arrears; and
- (iv) a lack of transparency in the way fees and charges are applied to accounts;

(b) the inability to seek effective redress through an accessible or efficient mechanism;

(c) poor customer service; and

(d) the imposition of excessive costs of credit (both in terms of interest rate charged and the amount of fees and charges applied to the account).³⁰

The conclusion reached by the DTI is that the CCA 1974 no longer provides adequate protection for all consumers. Dynamic changes in the consumer credit market over the past thirty years have not been matched by changes in the legislation intended to protect consumers from abuse:

²⁹ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004, p.31

³⁰ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004, p.5

The rights that the Act accords to consumers and the avenues it provides to them to challenge unfair conduct are restricted. Furthermore, the Act has provided regulators with insufficient powers to tackle improper or unfair conduct by consumer credit businesses.

The vast majority of consumer credit businesses do treat consumers fairly and reasonably and comply with their statutory obligations. These businesses resolve disputes informally and quickly and take effective steps to rectify instances of non-compliance. However, a small proportion of businesses do not, often with devastating consequences for individual consumers. The current weaknesses in the Act have allowed these unscrupulous consumer credit businesses to exploit the difficulty consumers have in obtaining redress so as to act unfairly or in breach of general standards of good conduct, and inflict considerable harm on consumers.³¹

B. Specific problems with obtaining redress

1. Extortionate credit

According to the DTI, the extortionate credit provisions of the CCA 1974 (Sections 137 - 140) have not provided consumers with effective redress:

Under the Act, a court may re-open a credit agreement to alter its terms or to set it aside where it is found to be part of an ‘extortionate’ credit bargain. Within the constraints imposed by issues of access to justice, this test has not served to enable consumers to seek effective redress. This means that consumers are unable and unwilling to challenge ‘extortionate’ conduct by lenders and means that some unscrupulous lenders may persist with exploitative practices.

In the 27 years of the Act’s operation, we understand that very few consumers have succeeded in having a court reopen a credit agreement on the basis that it is part of an extortionate credit bargain. There are only about 30 published court judgments that we are aware of where a court has considered the issue, although we are aware that the issue has been raised in proceedings more frequently.³²

The DTI identified a number of factors which contribute to the limited use of the ‘extortionate’ test to reopen a regulated credit agreement, including:

- too narrowly focussing the test on the cost of credit rather than the fairness of all the terms of the agreement;
- the current standard of ‘extortionate’ is too high to effectively deter practices that are unfair or exploitative;

³¹ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004, p.3

³² Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004, p.29

- the difficulty of bringing claims to court - many consumers are deterred by the expense, risk and complexity of bringing a case to court, for which legal aid is not generally available.

These factors restrict the effectiveness of the CCA 1974 for consumers by inhibiting private enforcement.³³

2. Licensing of consumer credit businesses

A criticism of the current credit licensing regime is that while the test used by the OFT to determine whether a person is fit to hold a credit licence gives particular weight to evidence of past failings, it does not expressly take into account a trader's ability to conduct their credit business in a fit manner in the future (for example, by ensuring staff are properly trained or adequate systems have been put in place).³⁴

The DTI suggests that this problem is compounded by limitations on the OFT's powers to investigate ongoing activities of the licensee:

If a trader behaves in a way, which, although undesirable, does not breach a specific provision of the Act [CCA 1974], the OFT is powerless to gain the information it needs to consider properly whether the licence should be revoked. (Unacceptable methods of debt-collecting or sales practices which take advantage of the elderly are examples of such activities). Currently, the OFT relies, principally, on the applicants themselves or complaints from the public or local Trading Standards Departments (TSDs).³⁵

It is the Government's view that the licensing system needs to be strengthened to ensure that the 'fitness' test used by the OFT takes into account an applicant's competence and preparedness to run a credit business as well as their past conduct (comparable to Financial Services Authority (FSA) procedures). It also needs to be updated so as to cover new credit activities (such as credit repair) which are not covered by current categories of licensable activity.³⁶

3. Enforcement and sanctions

At present the CCA 1974 provides few flexible enforcement options and sanctions. The OFT cannot do anything other than seek to revoke, vary or suspend the licence of a non-compliant consumer credit business, and has few powers to compel consumer credit

³³ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004, p30

³⁴ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

³⁵ Ibid

³⁶ Department of Trade and Industry, *Consultation on the licensing regime of the Consumer Credit Act 1974*, January 2003: <http://www.dti.gov.uk/ccp/consultpdf/credlic.pdf>

businesses to assist with its investigations. The OFT must amass a significant amount of evidence before issuing a minded to revoke notice (MTR).

A refusal, suspension or revocation may put the licensee out of business and, therefore, is only used in the most serious of cases. In 2001-2002, the OFT refused 27 of 16,293 applications for a licence and 20 of 11,974 renewal applications, it also revoked 19 of an estimated 205,000 active licences.³⁷

The OFT has developed informal practices, such as sending warning letters to licence holders and seeking undertakings about future practices, but those actions do not carry the same weight as a statutory power. While it is now possible to use Stop Now Orders in many cases to stop the offending conduct, they cannot be relied upon to cover all cases.³⁸

Commenting on the failings of the system, the DTI has said:

This means that enforcement of a type that does not relate to the most serious conduct is generally very difficult. Likewise consumers have few options available to them beyond the complaint and ADR systems maintained by consumer credit trade bodies (which we acknowledge to be effective in specific instances). The only other option is court action, which is expensive and intimidating for many consumers.³⁹

The information gathering powers of the OFT is also deemed to be inadequate. The CCA 1974 grants the OFT and Trading Standards Departments (TSDs) investigatory powers: to enter premises and inspect books and other records. However, these are limited to circumstances where the enforcement authority has reasonable cause to suspect that a breach of the CCA 1974 has been committed. They do not apply in respect of unfair business practices or other matters that, while not constituting a breach of the CCA 1974 could, nevertheless, have a bearing on a person's fitness to hold a licence.

Other regulators already adopt a more 'hands-on' approach to managing their licensing regimes. For example, the FSA continues to monitor newly authorised members, although there is no specific probation period. According to the DTI, a continuing process of fitness checking is desirable, with an enhanced system of sanctions where it is felt that the trader is not complying with his statutory obligations as a licence holder.⁴⁰

³⁷ Ibid

³⁸ Part 8 of the *Enterprise Act 2002* extends the scope of the Stop Now Order enforcement regime to include a wide range of domestic consumer protection legislation

³⁹ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004, p.20

⁴⁰ Department of Trade and Industry, *Consultation on the licensing regime of the Consumer Credit Act 1974*, January 2003: <http://www.dti.gov.uk/ccp/consultpdf/credlic.pdf>

III Review of consumer credit laws

A. In the UK – review of the CCA 1974

In its White Paper *Modern Markets: Confident Consumers*, published on 22 July 1999, the Government stated its intention to bring consumer credit legislation up to date so that it provides appropriate consumer protection.⁴¹ A discussion document was duly published in March 2000.

A Taskforce on Tackling Over-Indebtedness was set up in October 2000. Its remit is to address concerns about consumer debt in the UK by considering ways of achieving more responsible lending and borrowing.⁴²

On 1 July 2001, the DTI published a consultation document, *Tackling loan sharks and more!*, in which it sought views on the effectiveness of the existing regulation of information disclosure, early settlement, unfair credit transactions, consumer credit licensing, the financial limit above which agreements are not regulated under the CCA 1974 and consumer redress.⁴³ Announcing the start of this public consultation, Melanie Johnson, then the Consumer Minister, said:

Our credit laws are 30 years old and need a radical overhaul to protect people in today's credit market. This is a top priority for the Government.

There has been a worrying increase in the numbers of people falling into the debt trap, getting loans at often extortionate rates which they clearly can't afford to repay.

Consumers need to know what they are letting themselves in for when they sign up for credit. The expensive catch shouldn't be hidden in microscopic text. It should be explained, up front, by the lender.

We will take action to protect vulnerable consumers who are preyed on by rogue traders and make sure that consumers get clear and understandable information so they know exactly what they are getting into before they sign on the dotted line.⁴⁴

The publication of a number of wide-ranging public consultation documents followed. A full list is provided in the Appendix to this Research Paper.

⁴¹ Department of Trade and Industry White Paper, *Modern Markets: Confident Consumers*, Cm 4410, 22 July 1999

⁴² The Taskforce on Tackling Over-indebtedness has reported twice to Ministers and many of their recommendations were incorporated in the DTI's White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

⁴³ DTI consultation document, *Tackling loan sharks and more!*, 1 July 2001. A summary of responses was published by the DTI in February 2002 (see the Appendix to this Paper)

⁴⁴ Department of Trade and Industry press notice P/2001/398, *Johnson announces biggest overhaul of credit laws for a generation*, 25 July 2001

The White Paper, *Fair Clear and Competitive - the consumer credit market in the 21st century*, was published in December 2003.⁴⁵ In this paper, the Government concluded that the CCA 1974 was becoming out of date in the context of a diverse and complex consumer credit market:

The laws governing this market were set out a generation ago. In 1971, there was only one credit card available; now there are 1,300. 30 years ago, £32m was owed on credit cards; now it is over £49bn.

The regulatory structure that was put in place then is not the same as the regulatory structure required today. As the credit market has developed, reforms have become necessary to modernise the current regime and update it for the 21st century.⁴⁶

The White Paper outlined plans to use both secondary and primary legislation to improve the regulation of consumer credit. Commenting on this reform package, Patricia Hewitt, Secretary of State for Trade and Industry and Minister for Women and Equality, said:

New protections will go hand in hand with a series of changes to promote a more open, competitive market, offering more choice and less restriction.

This White Paper proposes a range of legislative changes relevant to the credit market of today. It will be regulated in a way that provides consumers with choice, information and protection at the right time. It also outlines our plans for a strategic approach to minimising over-indebtedness and improving financial inclusion by educating consumers; providing easier access to financial advice; and ensuring access to affordable credit.⁴⁷

On the same date, 8 December 2003, the DTI published a consultation document, *Establishing a Transparent Market*, which sought comments on those legislative changes that could be achieved through secondary legislation.⁴⁸ Subsequently, the following Statutory Instruments were laid before Parliament:

- *Consumer Credit (Disclosure of Information) Regulations 2004* – to ensure that contract terms and conditions in credit agreements are fair and written in plain English.⁴⁹

⁴⁵ This White Paper can be viewed on the DTI website at:

<http://www.dti.gov.uk/ccp/topics1/pdf1/creditwp.pdf>

⁴⁶ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

⁴⁷ HC Deb 8 December 2003 c.74WS

⁴⁸ The consultation document can be viewed on the DTI website at:

<http://www.dti.gov.uk/ccp/topics1/pdf1/creditpiu.pdf> Responses to the document can also be viewed at:

<http://www.dti.gov.uk/ccp/topics1/pdf1/creditconres.pdf>

⁴⁹ SI 2004 No. 1481

- *Consumer Credit (Agreements) (Amendment) Regulations 2004* – to introduce one set of rules for paper and electronic communications concluding credit agreements.⁵⁰
- *Consumer Credit (Early Settlement) Regulations 2004* – to introduce a more accurate formula for determining an early settlement figure than Rule 78 and details of early settlement rights to appear on the face of the credit agreement.⁵¹
- *Consumer Credit (Advertisements) Regulations 2004* – to ensure clearer and more understandable credit agreements.⁵²
- *The Consumer Credit (Miscellaneous Amendments) Regulations 2004*.⁵³
- *The Consumer Credit 1974 (Electronic Communications) Order 2004* – to enable the use of electronic communications for concluding regulated agreements and when sending notices and documents.⁵⁴
- *The Consumer Credit (Enforcement, Default and Termination Notices) (Amendment) Regulations 2004* - to ensure that all such notices sent under the Regulations are sent in paper format.⁵⁵

The remaining proposed reforms (relating to unfair credit relationships, consumer credit licensing, the financial limit and consumer redress), identified as being necessary in the White Paper but requiring primary legislation, are to be implemented by this *Consumer Credit Bill*. The Government hopes that the reforms already introduced by the new 2004 regulations and those to be implemented by this Bill will lead to higher standards of behaviour in the consumer credit market to the benefit of consumers.⁵⁶

The most recent development, a joint DTI and Department for Work and Pensions Paper, “*Tackling over-indebtedness – Action Plan 2004*”, was published on 20 July 2004.⁵⁷ There is also an inquiry by the Treasury Select Committee into the transparency of credit card charges.⁵⁸

B. In Europe – new proposals affecting consumer credit

The UK and other Member States have found the 1987 *Consumer Credit Directive* 87/102/EEC inadequate to regulate the EU credit market.⁵⁹ A major criticism of the

⁵⁰ SI 2004 No. 1482

⁵¹ SI 2004 No. 1483

⁵² SI 2004 No. 1484

⁵³ SI 2004 No. 2619

⁵⁴ SI 2004 No. 3236

⁵⁵ SI 2004 No. 3237

⁵⁶ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The consumer credit market in the 21st century*, Cm 6040, 8 December 2003

⁵⁷ This document can be viewed on the DTI website at:
<http://www.dti.gov.uk/ccp/topics1/pdf1/overdebt0704.pdf>

⁵⁸ http://www.parliament.uk/parliamentary_committees/treasury_committee/tc050803.cfm

⁵⁹ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The consumer credit market in the 21st century*, Cm 6040, 8 December 2003

directive is that it sets only the minimum requirements necessary for regulation across the EU. This has led to competitive distortions in the EU credit markets, thereby restricting consumer access to buy credit in other Member States.

The European Commission has brought forward two proposals aimed at strengthening consumer protection and establishing a single market in consumer credit: a revised Consumer Credit Directive and a draft Unfair Commercial Practices Directive. For the UK these proposals will have an important impact on consumer credit regulation:

A revision of existing law is an opportunity for the UK credit industry (worth 40% of the EU credit market which exceeds £500bn⁶⁰) to expand with legal certainty and create an environment where consumers can cross borders to shop for credit with confidence.⁶¹

1. Revised Consumer Credit Directive

The draft Consumer Credit Directive was published by the European Commission in September 2002.⁶² This aims to harmonise fully the laws on consumer credit in the Member States and to facilitate the provision of cross-border services. According to the UK Government, there are certain issues the directive must address if it is to be effective, including:

- fair and equal cross-border data access and exchange;
- the adoption of a EU-wide approach to regulation of consumer credit information;
- advertising and unfair practices;
- common rules on APR calculations;
- barriers to cross-border debt collection and recovery practices;
- an effective out-of-court redress mechanism; and
- an effective ‘passport’ regime for lenders wishing to market and sell credit products cross-border.⁶³

The Government has said that it will work closely with the European Commission, other Member States and the European Parliament to ensure that the revised directive works in the best interests of the UK.⁶⁴ In the meantime, the Government has decided to go ahead with reform of the CCA 1974; it does not believe it would be right to hold up domestic reform until the directive is agreed. It expects UK regulation to be consistent with and to complement European legislation.

⁶⁰ Consumer Credit Directive Proposal – explanatory memorandum COM(2002) 443 final

⁶¹ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer credit market in the 21st century*, Cm 6040, 8 December 2003

⁶² COM (2001) 443 final

⁶³ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer credit market in the 21st century*, Cm 6040, 8 December 2003

⁶⁴ Ibid

2. Draft Unfair Commercial Practices Directive

On 18 June 2003, the European Commission published a draft directive as a harmonisation measure on Unfair Commercial Practices in the field of consumer protection.⁶⁵ It is to cover all business sectors, including consumer credit.

The draft directive contains a prohibition on unfair commercial practices. A practice will be deemed unfair if it is contrary to ‘professional diligence’ (i.e. the care and skill exercised by a trader in accordance with usual market practice) and materially distorts (or is likely to materially distort) the economic behaviour of a consumer. It highlights two principal categories of unfair commercial practices:

- misleading commercial practices (actions as well as omissions); and
- aggressive commercial practices.

In each case, the directive sets out criteria to establish whether a practice is misleading or aggressive and includes an annex containing a non-exhaustive list of examples of unfair commercial practices intended to demonstrate further application of the criteria.

The DTI has concerns about the possible impact of this proposed directive on highly-regulated sectors such as financial services, and is consulting separately on it:

The Government is concerned about the possible impact of this cross cutting measure on already highly regulated sectors such as financial services. The Government’s broad objectives in future negotiations will be to ensure that any Directive offers effective consumer protection, avoids duplication of regulation, and provides legal certainty for business, consumers and enforcement bodies. The Directive should also complement the provisions of the CCD [Consumer Credit Directive] and the UK reform process through its coverage of marketing and selling practices. The Government has consulted separately on this proposal.⁶⁶

IV Main provisions of the Bill

The main aim of the *Consumer Credit Bill* is to reform the CCA 1974 under four broad headings:

- A. To enhance consumer rights and redress - by replacing the current ‘extortionate credit’ test with a new test based on unfairness, and by introducing an Alternative Dispute Resolution (ADR) scheme.

⁶⁵ COM (2003) 356 final

⁶⁶ Department of Trade and Industry White Paper, “*Fair, Clear and Competitive – The consumer credit market in the 21st century*”, Cm 6040, 8 December 2004. See also the Government’s consultation on the draft *Unfair Commercial Practices Directive*: <http://www.dti.gov.uk/ccp/consultpdf/unfaircon.pdf>

- B. To strengthen the regulation of consumer credit businesses - by creating a more targeted credit licensing regime and equipping the OFT with new powers (by way of intermediate sanctions) to take action against rogue traders, including financial penalties.
- C. To extend regulation to all types of consumer credit and hire agreements (subject to limited exemptions) – by abolishing the financial limit that currently restricts protection under the CCA 1974 to loans of £25,000 or less.
- D. To provide debtors with new post-contractual information.

A. Improving Consumer rights and redress

1. Unfair relationships

This section should be read in conjunction with Part I (page 9) and Part II (page 16) of this Paper.

A primary aim of the Bill is to ensure greater fairness in the creditor-debtor relationship.

The Bill seeks to repeal the extortionate credit provisions of the CCA 1974 (sections 137-140) and replace them with a new ‘unfair relationship test’.⁶⁷ This new test (i.e. that a consumer credit business should not behave unfairly) is intended to provide a single standard of conduct to all consumer credit businesses which is consistent with industry codes and Financial Services Authority (FSA) regulation.

Specifically, **clause 19** inserts into the CCA 1974 a new section 140A. This new section 140A would enable the court to make an order if it finds that the relationship between the creditor and the debtor arising out of a consumer credit agreement is unfair to the debtor. This new ‘unfair relationship’ test would cover the entire consumer credit relationship; rather than be simply an assessment of the terms of the agreement and whether they allow for extortionate costs.

Whether a regulated credit agreement is unfair to the debtor would be determined by the court by reference to all the relevant circumstances including:

- any of the terms of the agreement or of any related agreement;
- the way in which the creditor has exercised or enforced any of his rights under the agreement or any related agreement;
- any other thing done (or not done) by, or on behalf of, the creditor (either before or after the making of the agreement or any related agreement).⁶⁸

⁶⁷ Clause 22(3) of the Bill

⁶⁸ New section 140A(1) inserted into the CCA 1974 by clause 19 of the Bill

Additionally, the court could take into account any other matters it thinks relevant (including matters relating to the specific circumstances of the creditor and debtor in question).⁶⁹ If it decides in favour of the debtor, the court could do one or more of the following:

- (a) Require the creditor, or any associate or former associate of his, to repay (in whole or in part) any sum paid by the debtor or by a surety by virtue of the agreement or any related agreement (whether paid to the creditor, the associate or the former associate or to any other person);
- (b) require the creditor, or any associate or former associate of his, to do or not to do (or to cease doing) anything specified in the order in connection with the agreement or any related agreement;
- (c) reduce any sum payable by the debtor or by a surety by virtue of the agreement or any related agreement;
- (d) direct the return to a surety of any property provided by him for the purposes of a security;
- (e) otherwise set aside (in whole or in part) any duty imposed on the debtor or on a surety by virtue of the agreement or any related agreement;
- (f) alter the terms of the agreement or of any related agreement;
- (g) direct accounts to be taken, or (in Scotland) an accounting to be made, between any persons.⁷⁰

However, an order may only be made in connection with a regulated credit agreement following an application to the court made by the debtor (or his surety); or at the request of the debtor (or his surety) in any enforcement proceedings brought by the creditor; or at the request of the debtor (or his surety) in any proceedings where the amount paid or payable under the agreement is relevant.⁷¹ If it is alleged by the debtor (or his surety) that the credit relationship is unfair, it is for the creditor to prove the contrary.⁷²

The types of agreement covered by this new ‘unfair relationships’ test are defined by new section 140C inserted into the Act by **clause 21**. Basically, any regulated agreement that involves the provision of credit to an individual would be covered. The test would also cover the practice where the creditor enters into successive credit agreements with a debtor for the purpose, for example, of increasing the total amount of the debt or

⁶⁹ New section 140A(2) inserted into the CCA 1974 by clause 19 of the Bill

⁷⁰ New section 140B inserted into the CCA 1974 by clause 20 of the Bill

⁷¹ New section 140B(2) inserted into the CCA 1974 by clause 20 of the Bill

⁷² New section 140D(4) inserted into the CCA 1974 by clause 22 of the Bill

obtaining multiple fees from the debtor for setting up each loan. However, the ‘unfair relationships test’ would not apply to consumer credit agreements secured on land that are already regulated by the FSA under FSMA 2002.⁷³

The DTI has said that the new test will have some retrospective effect:

The new unfair relationships test will apply to all new credit agreements made after the date that the reforms commence and will apply to any agreements already made which continue in existence at a specified date after commencement. We will consult with consumers and industry as to when this date will be.

The period between the commencement date and the specified date will be a transitional period, to allow creditors to ensure that any agreements that will continue beyond the end of the transitional period comply with the new test.

The old test will continue to apply to agreements that have been completed (e.g. no party has any further obligations under the agreement because no further sums are payable) before the end of the transitional period. The new unfair relationships test will not apply to these agreements.⁷⁴

Part 8 of the *Enterprise Act 2002 (EA 2002)* empowers the OFT to bring proceedings against a person who, as a consequence of a breach of a statutory obligation, harms the ‘collective interest’ of consumers. Under **clause 22** of the Bill, the OFT would be required to give advice about the interaction between the provisions on unfair relationships and Part 8 of the EA 2002.⁷⁵ (For example, it may choose to publish guidance on practices that could give rise to an unfair relationship between creditors and debtors).

2. Compulsory Alternative Dispute Resolution (ADR) scheme

Clauses 59 to 61 and **schedule 2** of the Bill would provide consumers with free access to an ADR scheme to be run by the existing Financial Ombudsman Service (FOS). The DTI hopes that both for consumers and businesses, the new ADR procedure will provide a quick, efficient and easy resolution of consumer disputes, at considerably less cost than court action.

The FOS was set up as an independent dispute resolution service under Part 16 of the *Financial Services and Markets Act 2000 (FSMA 2000)*. The FOS, which is free to consumers, already deals with disputes about mortgages, other loans and credit cards

⁷³ Consumer credit agreements secured on land are exempt under section 16(6c) of the CCA 1974. Such agreements are regulated by the Financial Services Authority and the *Financial Services and Markets Act 2000*

⁷⁴ Department of Trade and Industry, *Questions and Answers on the Consumer Credit Bill*, December 2004: <http://www.dti.gov.uk/ccp/creditbill/pdfs/creditbillqa.pdf>

⁷⁵ New section 140D inserted into the CCA 1974 by clause 22 of the Bill

between consumers and firms regulated by the FSA. Under the Bill's new provisions, the FOS will acquire a broad jurisdiction to determine consumer credit complaints and its decisions will be capable of enforcement by the courts.⁷⁶ Although no appeal system is provided for, its decisions are already subject to judicial review.

The ADR procedure would be mandatory for all consumer credit businesses operating under a standard licence under the CCA 1974; the scheme would not apply to unlicensed credit businesses or those covered by group licences.⁷⁷ Creditors would have a legal duty to refer complaints to the FOS where a debtor requests this; debtors will not have to pay at all and will have disputes determined by an independent adjudicator.

The detailed operation of the new ADR procedure would be determined largely by rules ('consumer credit rules') to be made by the FOS after public consultation and approval by the FSA.⁷⁸ The FOS would also be allowed to specify a maximum limit for compensation that can be awarded under its consumer credit jurisdiction.⁷⁹

Before a complaint to the FOS can be made, the complainant (either an individual or a surety) must meet the relevant eligibility criteria set by the CCA 1974 and the FOS.⁸⁰ In addition, the ADR scheme would only be available once a consumer has complained to the credit business's own complaints-handling mechanism, and has exhausted all relevant avenues for redress.⁸¹ If the complaint could be dealt with under the FOS's existing compulsory jurisdiction it would not be dealt with under its consumer credit jurisdiction. In practice, this would mean that a complaint involving an FSA authorised firm engaged in a consumer credit activity will be covered by FSA rules under section 226 of the FSMA 2000, rather than FOS rules under new section 226A of the same Act.⁸²

The cost of establishing and running the new consumer credit jurisdiction of the FOS will be met by an annual levy to be imposed by the FOS on all relevant businesses but collected by the OFT at the same time as it collects the credit licence fee.⁸³ The FOS may also include a fee to cover the costs of collection.⁸⁴ However, the first two complaints about a particular business handled by the FOS would not require the payment of a case fee.

A contravention by a licence-holder of any provision relating to the consumer credit jurisdiction may be considered by the OFT in determining that person's fitness to hold a

⁷⁶ Schedule 2 16D of the Bill

⁷⁷ New section 226A(2) and (3) of the FSMA 2000 inserted by clause 59 of the Bill

⁷⁸ New section 226A(7) of FSMA 2000

⁷⁹ Clause 61(5) of the Bill

⁸⁰ New section 226A(4) of the FSMA 2000 inserted by clause 59 of the Bill

⁸¹ New schedule 2 part 3A and schedule 17 to the FSMA 2000, section 16B(1)

⁸² New section 226A(f) of the FSMA 2000 inserted by clause 59 of the Bill

⁸³ New section 234A inserted into Part 16 of the FSMA 2000 by clause 60 of the Bill

⁸⁴ New section 234A(2) inserted into the FSMA 2000 by clause 60 of the Bill

licence. The Bill amends section 353 of the FSMA 2000 to allow the FOS to disclose information about cases and decisions to the OFT to assist the OFT to discharge its licensing functions under the CCA 1974.

The Finance and Leasing Association (FLA) has already questioned the necessity for introducing a mandatory ADR scheme (see Part V of this Paper page 50).⁸⁵ The DTI acknowledges that there are already a number of informal dispute resolution schemes run by trade associations that currently provide an option other than the courts for some consumer credit disputes. However, in its view there are a number of reasons why a new mandatory ADR scheme should be introduced:

The existing schemes are effective but they are voluntary and are not universal in their application of the Act [the CCA 1974] and consumers may be wary of taking their dispute to an industry body whom they may perceive as being ‘on the side of’ the business about which they are complaining. An independent ADR scheme that covers all licensed consumer credit business is desirable.⁸⁶

The DTI believes that there are several advantages in using the FOS for ADR as opposed to establishing a new body to perform this function:

- certain consumer credit licence holders are already subject to its jurisdiction for their FSA regulated activities, such as banks and building societies;
- consumer credit firms that arrange insurance will be subject to FSA regulation from January 2005 when the Insurance Mediation Directive is implemented;
- if a separate body were to be established for ADR, a complaint involving a consumer credit product and payment protection insurance would be split between the FOS and the new body;
- the FOS is a member of Fin-Net, the court-of-court complaints network for retail financial services.⁸⁷

According to the Government, its intention in implementing both a new ‘unfairness test’ and an ADR scheme is to:

...improve the ability of consumers to seek redress, make it easier for borrowers and consumer credit businesses to resolve disputes in a speedy, fair and

⁸⁵ Finance and Leasing Association, *FLA’s response to DTI’s consultation document on the provision of ADR for disputes arising under the Consumer Credit Act 1974*, 16 March 2004. This can be viewed at: http://www.fla.org.uk/fla_home/Consultation_Papers/Responses%20to%20ADR%20Consultation.doc

⁸⁶ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, December 2004, p 31

⁸⁷ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

proportionate manner, and act as an incentive to compliance with the procedural requirements of the Act [the CCA 1974] and the enhanced licensing regime.⁸⁸

B. Improving the regulation of consumer credit businesses

This section should be read in conjunction with Part I (page 10) and of Part II (page 17) of this Paper.

1. Creating a more targeted credit licensing regime

The CCA 1974 is underpinned by a credit licensing system administered by the OFT. This licensing system will be reformed by the Bill to bring it closer to the system of authorisation operated by the FSA under FSMA 2000. The OFT will have wider information gathering powers to determine whether a credit provider is fit to hold a licence. There will be a more vigorous ‘fitness’ test for assessing the suitability of applicants and the OFT will have powers to ensure the ongoing fitness of licence holders. The OFT will adopt a risk-based approach to monitoring. In addition, it will have new powers to impose conditions on licence holders and to request undertakings.

a. Applications for standard licences

Clause 28 of the Bill inserts a new section 24A into the CCA 1974. The aim of this new section is to enable the OFT to manage the standard licence application process more efficiently by requiring people to specify in applications exactly what type of business they want the licence to cover. Specifically, the applicant would be required to state whether he is applying –

- (a) for the licence to cover one or more consumer credit business, consumer hire business and ancillary credit business generally (with no limitation); or
- (b) for the licence only to cover one or more limited descriptions of business within any of the broad categories of consumer credit business, consumer hire business and ancillary credit business. (The OFT is to specify the descriptions of business within these broad business categories).

It would be for the applicant to define the breadth of licence he requires. The benefit is that the OFT will have to assess ‘fitness’ to hold a licence only in relation to specified activities within the licensable categories of business. In turn, the applicant will have to satisfy the OFT about his fitness only for the particular sector in which he wishes to operate. Commenting on the potential benefits of this reform to the credit licensing system, the DTI has said:

⁸⁸ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, December 2004, p 29

Although they may be working in diverse areas of the credit market, at present, traders are assessed in much the same way. By clarifying these different categories, and the levels of risk attached to them, the OFT will be able to target its resources more effectively (for example, more questions might be asked of a specialist finance broker than a high street retailer).⁸⁹

When determining an applicant's fitness to hold a standard credit licence, the OFT would be required under **clause 29** of the Bill to consider:

- the skills, knowledge and experience (in relation to consumer credit, consumer hire or ancillary credit business) of the applicant and anyone who will work for him under that licence; and
- the practices and procedures that will be implemented in connection with the business.⁹⁰

This is in addition to the current requirements under the CCA 1974 for the OFT to consider evidence of past misconduct or offences.⁹¹

The effect of clause 29 is to broaden the 'fitness test'; the OFT would be able to look at an applicant's past track record for misconduct and other offences, and also assess his competence and his preparedness for running a credit business.⁹²

If an applicant satisfies the OFT that he is fit to do everything he has applied for, he would be entitled to a licence to do that. If not, there is a power for the OFT to issue him with a more limited licence.⁹³ The OFT would be required under the Bill to publish guidance as to the way it will determine the fitness of a person to hold a licence.⁹⁴

Already, under sections 30 and 31 of the CCA 1974, licences can be varied by the OFT either on application or compulsorily, whilst section 32 of the CCA 1974 gives the OFT the power to suspend or revoke licences. Under **clause 31** of the Bill, the OFT cannot extend the scope of a licence by compulsory variation.

Under **clause 32** of the Bill, if the OFT decides not to renew a particular licence, to renew a licence on different terms to the application, or to compulsorily vary or revoke or suspend a licence, the OFT would be able to defer that action to allow the licensee to transfer or wind up its business or any part of it.⁹⁵ The OFT would issue a notice requiring an application for deferral by the licensee within a specified period. If the licensee wished

⁸⁹ Department of Trade and Industry, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

⁹⁰ Clause 29 of the Bill amends section 25 of the CCA 1974

⁹¹ See Part II of this Paper, page 10

⁹² FSA regulated firms are already deemed 'fit' by definition

⁹³ Sections 25(1) to (1AD) of the CCA 1974 as amended by clause 29 of the Bill

⁹⁴ New section 25A inserted into the CCA 1974 by clause 30 of the Bill

⁹⁵ New section 34A inserted into the CCA 1974 by clause 32 of the Bill

to act on this notice, he would have to make an application for deferral within the period specified in that notice. An applicant may appeal against a refusal by the OFT to defer its licensing action.

b. *Definite and indefinite standard licences*

Clause 34 allows the OFT to move away from its current five-yearly licence renewal process to a new system of indefinite standard licences with periodic payments to maintain the licence. The Government hopes that this reform will significantly reduce the current administrative burden on businesses and enable the OFT to target those businesses and sectors which propose the greater risk to consumers.⁹⁶

A standard licence would be valid indefinitely unless-

- a) the application for its issue requests that it have effect for a limited period only; or
- b) the OFT thinks there is good reason why it should have effect for a limited period only.

However, group licences would have effect for a limited period only (normally renewable every five years) unless the OFT thinks there is a good reason why it should have effect indefinitely. This is to allow the OFT to oversee the activities of the group licence holder, who is responsible for ensuring that members of the group are fit to operate in the consumer credit market.

Under **clauses 35 to 37** of the Bill, the current licence renewal fee is replaced with a periodic licence fee payable to the OFT. The OFT can extend payment periods in respect of indefinite licences if it believes there is good reason for doing so. However, failure to pay a periodic charge in respect of a standard licence during the payment period (or extended payment period) could result in the licence being terminated.⁹⁷

c. *The provision of new information*

At the moment, the OFT and Trading Standards Departments (TSDs) have only limited powers when trying to establish whether a trader is fit to hold a consumer credit licence (see Part II of this Paper page 18).

Clauses 44 to 51 of the Bill would enhance the OFT's powers of investigation so that it could, by notice, insist on seeing any relevant information held by applicants, licensees (of both standard and group licences) and, in specified circumstances, third parties. These

⁹⁶ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

⁹⁷ Details of licences terminated for this reason must be kept on the OFT's public register

powers may include the requirement to produce books, documents and records, along with powers to carry out compliance visits where there is particular concern.

Licensees would also be required to notify the OFT, within 28 days of their becoming aware, of any material change in circumstances relating to their fitness to hold a licence.⁹⁸

Clauses 47 and 48 of the Bill would also enable the OFT to enter premises (other than those used solely as a dwelling) on reasonable notice, and to apply for a warrant to enter and search when a notice requesting information has not been complied with.⁹⁹

Failure to comply with an information requirement under the new section 36B or a request to gain access to premises under new section 36C, could result in the OFT applying to the court for an enforcement order.¹⁰⁰

2. Intermediate sanctions - new OFT powers to impose requirements

a. Scope of the new intermediate sanctions

A major criticism of the current licensing system under the CCA 1974 is that it fails to provide the OFT with sufficient powers to tackle improper or unfair conduct by consumer credit businesses (see part II of this Paper page 17).

To remedy this failing, clauses 38 to 43 of the Bill would provide the OFT with new powers to apply intermediate sanctions to tackle behaviour which causes detriment to consumers but which does not render a business ‘unfit’.

Clause 38 inserts a new section 33A into the CCA 1974. This new section applies where the OFT is dissatisfied with any matter in connection with –

- a business being carried on, or which has been carried on, by a licensee or by an associate or a former associate of a licensee;
- a proposal to carry on a business which has been made by a licensee or by an associate or a former associate of a licensee; or
- any conduct not covered by paragraph (a) or (b) of a licensee or of an associate or a former associate of a licensee.

Under this new section, the OFT could, by notice impose special conditions on (or take undertakings from) licensees in order to address unfit conduct. These special conditions would be specific to a particular licence-holder, to ensure that the business is meeting its fitness requirements (for example, a training requirement). A breach of a condition could

⁹⁸ Clause 45 of the Bill

⁹⁹ Clauses 47 and 48 of the Bill insert new sections 36C and 36D respectively into the CCA 1974

¹⁰⁰ New section 36E inserted into the CCA 1974 by clause 49

lead to the licence-holder having a financial penalty imposed by the OFT, or ultimately the revocation, suspension or variation of his licence.

In relation to group licences, **clause 39** inserts a new section 33B into the CCA 1974. This new section deals with the power of the OFT to impose special conditions on the so-called ‘responsible person’ where the OFT is dissatisfied with the way in which that person is regulating (or has regulated) the conduct of the group.

For the purposes of the Bill, a person is a ‘responsible person’ in relation to a group licence if he is the original applicant under it and he has responsibility (whether by virtue of an Act, an agreement or otherwise) for regulating or otherwise supervising persons who are licensees under the licence.

Again, the OFT may, by notice to the responsible person, require him to do, stop, or not to do anything specified in the notice in order to either correct the matters giving rise to the OFT’s concern, or to ensure that the same or similar matters do not arise in the future.

Clause 40 of the Bill inserts yet another new section, section 33C, into the CCA 1974. This new section is significant because it empowers the OFT to vary or revoke special conditions on its own motion or on application by the licence-holder or any person named in a requirement and in some material way affected by it (for example, by being prevented from being employed by the person on whom the requirement is imposed, or restricted as to the activities that he may engage in as an employee).

The OFT must follow a strict procedure when imposing conditions. This is set out in new section 33D inserted into the Act by **clause 41** of the Bill. In essence, a decision to impose a special condition (or undertaking) or financial penalty would be subject to the same procedural safeguards as a decision to refuse, revoke or vary a credit licence. Under **clause 43** of the Bill, there would be a right of appeal for persons on whom a condition is imposed (and affected persons) against imposition, variation or revocation of a condition by the OFT.

The OFT would be required under the Bill to issue guidance as to how it exercises or how it proposes to exercise its powers in relation to the imposition, variation or revocation of special conditions.¹⁰¹ It would also be required to record special conditions and details of their variation in a public register.

b. New OFT powers to impose civil penalties

Clause 50 inserts new section 39A into the CCA 1974. This new section would empower the OFT to impose civil penalties on persons who do not comply with a condition imposed by the OFT under:

¹⁰¹ New section 33E inserted into the CCA 1974 by clause 42 of the Bill

- new intermediate power to impose requirements on licensees (new section 33A);
- new power to impose requirements on a group licence (new section 33B); or
- new duty on licensees to notify OFT of certain changes to their circumstances (new section 36A).¹⁰²

If a person has failed to comply with such a condition, then the OFT may, by first issuing a penalty notice, impose a penalty of up to £50,000 per breach.¹⁰³

A penalty notice must contain the following information:

- the OFT's reasons for deciding that a person is liable to a penalty;
- the amount of the penalty that is being imposed and how this figure was determined;
- how the payment of the penalty may be made; and
- the period within which the penalty must be paid to the OFT (which should not be earlier than the end of the period during which an appeal may be brought against the imposition of the penalty).

Before imposing a fine, the OFT must have regard to any other steps which it has taken or it might take in relation to the conduct in question. Other options available to the OFT include revocation or suspension of a licence.

In respect of a group licence, the OFT must give a general notice of the imposition of a penalty on the responsible person in relation to a group licence. This must also include the OFT's reasons for deciding that the group is liable to a penalty, state the amount of the penalty to be imposed and set out the OFT's reasons for determining that amount.¹⁰⁴

Anyone who has had a civil penalty imposed on him by the OFT may appeal to the new Consumer Credit Appeals Tribunal (see below).

c. Consumer Credit Appeals Tribunal

Under the Bill, the appeals process against OFT decisions will be made more transparent for consumer credit and hire businesses than it is at present.

Clause 55 and **schedule A1** of the Bill would establish a new Consumer Credit Appeals Tribunal (CCAT) and give the Lord Chancellor the power to make its procedural rules.

¹⁰² Inserted into the CCA 1974 by clauses 38, 39 and 25 of the Bill

¹⁰³ The maximum penalty may be changed by an order by the Secretary of State (approved by an affirmative resolution of both Houses of Parliament)

¹⁰⁴ Clause 53 of the Bill

If the Bill is enacted, appeals in respect of decisions taken by the OFT under the CCA 1974 will be to the new CCAT and not to the Secretary of State (as is currently the case). The time limit for claims and the form of notice of appeal would be specified in the rules of the Tribunal.

If dissatisfied with the outcome of an appeal to the Tribunal, there would be a right of appeal to the Court of Appeal of England and Wales and Northern Ireland or to the Court of Session in Scotland.¹⁰⁵ However, the appeal must be on a point of law against a decision of the Tribunal. If the Appeal Court considers that the decision is wrong in law it may overturn or vary the decision, substitute a decision of its own for the decision of the Tribunal or return the matter back to the Tribunal for a rehearing and decision. Ultimately, an appeal may be made from the Courts of Appeal to the House of Lords with the leave (i.e. permission) of the court or the House of Lords.¹⁰⁶

By virtue of **clause 58(5)** of the Bill, the CCAT would be covered by the *Tribunals and Inquiries Act 1992* and as a consequence would be subject to the supervision of the Council on Tribunals.

C. Extending statutory regulation to all types of regulated agreements

A main aim of the Bill is to widen consumer credit protection.

1. Abolition of the financial limit

The purpose of the CCA 1974 is to protect consumers when entering into small-to-medium value credit or hire agreements. Currently, the CCA 1974 applies only to agreements where credit provided or the hire payments to be made do not exceed £25,000.

In its White Paper, the Government explained the reasons why it believes it is necessary to remove a financial limit to the CCA 1974:

...more and more consumer agreements are no longer regulated due to an increase in borrowing on second-charge mortgages and unsecured loans above £25,000.

In particular, consumers are being encouraged to use secured loans to consolidate unsecured debt. This reduces consumer's monthly payments but spreads their debt over a longer period of time, resulting in higher borrowing costs. In addition, once the borrowing is secured, they run the risk of having their property repossessed in the event of default.

¹⁰⁵ New section 41A inserted after section 41 into the CCA 1974 by clause 57 of the Bill

¹⁰⁶ Appeals from the Court of Session lie to the House of Lords by section 40 of *Court of Session Act 1988*

The lack of protection is further highlighted by the fact that from 31 October 2004, the FSA will be given the power to regulate first-charge mortgages, for which there will be no financial limit. However, the FSA will not regulate second-charge mortgages, so those loans above £25,000 would therefore remain unregulated if the financial limit of the CCA is not amended.¹⁰⁷

Clause 2 of the Bill would remove the financial limit: all consumer credit and consumer hire agreements would then be regulated by the CCA 1974 regardless of the amount of the credit or the amount of the hire payments, unless specifically exempted.

Those consumer credit or hire agreements exempt from regulation under the CCA 1974 are:

- first-charge mortgages (of no financial limit), which are already regulated by the FSA under the FSMA 2000;
- certain transactions involving high net worth individuals; and
- business lending above £25,000.

a. Exemption relating to high net worth individuals

For a credit or hire agreement involving a ‘high net worth’ individual to be exempt under the Bill, certain conditions must be met:

- the debtor or hirer must be a natural person (i.e. not a partnership, unincorporated association or body corporate);
- the agreement must include a declaration, in the specified form, that the debtor or hirer agrees to forego the protection and remedies that would be available under the CCA 1974 if the agreement was a regulated agreement; and
- a statement of ‘high net worth’, in a specified form, has been made in relation to him by a specified type of person (e.g. an accountant or solicitor).¹⁰⁸

This statement of high net worth must be current in relation to the agreement (i.e. drawn up no more than one year before the date of the making of the agreement). It must state that the debtor or hirer, in respect of the previous financial year (being the year ending 31st March preceding the current financial year in which the statement is made), either:

- received income of a specified description of the specified amount or more during that period; or

¹⁰⁷ Department of Trade and Industry White Paper, “*Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*”, Cm 6040, 8 December 2003

¹⁰⁸ New section 16A inserted into the CCA 1974 by clause 3 of the Bill. For the purposes of the Bill, ‘specified’ means specified by order of the Secretary of State

- had net assets of a specified description which were of a value not less than the specified amount during the whole of that period.

The ‘specified amount’ is to be determined by order of the Secretary of State.

In effect, the Bill permits ‘high net worth’ individuals who meet specific requirements in terms of their annual income or net assets to opt out of regulation under the CCA 1974 on the making of a declaration that they agree to forgo the protection of the Act. In the RIA of the Bill, the Government gave its reasons for making this exemption:

In respect of high net worth consumers, we have considered the concerns of industry that such consumers seeking large sums by way of personal borrowing would, if constrained by regulation under the Act, simply move their business to offshore financial centres with the consequences of a significant reduction in business for British consumer credit businesses.¹⁰⁹

b. Exemption relating to business lending

Clause 1 of the Bill substitutes a new definition of ‘individual’ in section 189(1) of the CCA 1974. ‘Individual’ would now include:

- a partnership consisting of two or three persons, not all of whom are bodies corporate; and
- an unincorporated body of persons which does not consist entirely of bodies corporate and is not a partnership.

So, partnerships of more than three members will not be covered by the CCA 1974 in respect of future borrowing or hire transactions (these partnerships will be exempt in the same way as bodies corporate for the purposes of the Act).

Clause 4 of the Bill exempts business credit and hire agreements from regulation under the CCA 1974 where the credit provided or hire payments to be made exceed £25,000.

For the purposes of clause 4, a credit or hire agreement will be presumed to be wholly or predominantly for business purposes where it includes a declaration by the debtor or hirer to that effect, unless at the time the agreement was made, the creditor or owner (or any other person acting on his behalf in relation to the agreement) knows or has reasonable cause to suspect that the declaration is not true. If there is any doubt as to whether an agreement is for a business purpose, all the circumstances of the proposed transaction will be taken into account.

¹⁰⁹ Department of Trade and Industry, *Full Regulatory Impact Assessment – Consumer Credit Bill*, November 2004

From this reading of clauses 1 and 4 of the Bill, it follows that regulation under the CCA 1974 will only extend to business lending of less than £25,000 in value provided to small businesses (i.e. sole traders, partnerships of three partners or less and other unincorporated bodies not consisting entirely of bodies corporate). Borrowing above £25,000 wholly for business purposes will not be protected by the CCA 1974.

c. Enforceability of regulated agreements in cases of infringement

Removing the financial limit also has a knock-on effect on the enforceability of regulated agreements in cases of infringement by the lender.

Section 127 of the CCA 1974 currently governs the enforceability of agreements and sets out the powers a court has to enforce a regulated agreement. In cases where certain requirements of the Act, relating to the form and content of an agreement, have not been followed by the lender, the court has discretion to consider whether to make an agreement enforceable.¹¹⁰ However, in certain instances, the court is prevented from making an enforcement order (i.e. the agreement will be automatically unenforceable) if the agreement is not properly executed (for example, the documents were not in a certain prescribed form or signed) or where the lender has failed to provide a cancellation notice in terms prescribed in the Act.¹¹¹

In its White Paper, the Government confirmed its view that removing the financial limit could expose lenders to greater liability where agreements are held to be unenforceable:

A more proportionate approach to enforcement will therefore be sought which will seek to balance, on the one hand, the objective of ensuring that particular attention is paid to the inclusion of certain terms in documentation signed by borrowers, and on the other, the financial consequences of unenforceability by lenders.¹¹²

Clause 15 of the Bill would give the court the discretion to determine whether agreements are enforceable regardless of the breach.

¹¹⁰ Sections 127(1) and (2) of the CCA 1974

¹¹¹ Sections 127(3) and (4) of the CCA 1974. See also *Wilson & Others v. Secretary of State for Trade and Industry* (Appellant) [2003] UKHL 40

¹¹² Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

D. Provision of new post-contractual information to consumers

The Government has recently introduced new Regulations about pre-contract disclosure and early settlement to improve the quality of the information consumers receive from consumer credit businesses.¹¹³

However, according to the Government's recent White Paper, a contributory factor identified in relation to the escalation of consumer debt has been the lack of ongoing information that many borrowers receive concerning their credit agreement:

This is of particular concern to consumers who fall into arrears, as they are often unaware of the consequences of charges on their account, default costs for missed payments, compound interest on the amount owed or underpayment on the accumulation of their debt.

At present, although the CCA 1974 contains some duties on the lender to provide information, these are generally only triggered by a request from the consumer. There is no obligation on a lender to provide regular statements or, crucially, to inform consumers when payments have been missed.¹¹⁴

The Bill now requires creditors to provide post-contractual information in relation to regulated fixed-sum credit and running account credit accounts.

Running-account credit can be defined as a facility under a personal credit agreement whereby the debtor is enabled to receive from time to time from the creditor (or a third party) cash, goods and services (or any of them) to an amount or value such that the credit limit (if any) is not at any time exceeded.¹¹⁵ The most common examples of running account credit agreements are bank overdrafts, credit card accounts and store card accounts.

Fixed-sum credit is any other facility under a personal credit agreement whereby the debtor is enabled to receive credit (whether in one amount or in installments).¹¹⁶ A fixed-sum credit agreement is for a definite amount (whether fixed at the time of the contract or determinable thereafter according to its terms), so that repayments will in due course result in the credit being discharged, and if the debtor wants fresh credit he has to negotiate a new agreement. Examples of fixed-sum credit agreements are hire-purchase, conditional sale, credit sale and fixed loan agreements (as opposed to overdraft).

¹¹³ *Consumer Credit (Advertisements) Regulations 2004; Consumer Credit (Agreements)(Amendment) Regulations 2004; Consumer Credit (Disclosure of Information) Regulations 2004; and the Consumer Credit (Early Settlement) Regulations 2004*

¹¹⁴ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

¹¹⁵ Section 10(1) of Part II of the CCA 1974

¹¹⁶ Section 10(2) of Part II of the CCA 1974

1. Annual statements to be provided in respect of regulated credit agreements

To ensure greater transparency for consumers, the Bill will require creditors to provide annual statements - at no direct cost to the consumer – detailing prescribed information about the account. The aim is that consumers will be kept informed of the status of their accounts throughout the life of the agreement.

a. For fixed-sum credit accounts

Clause 6 of the Bill, which inserts a new section 77A into the CCA 1974, requires consumer credit businesses to issue annual statements for all regulated fixed-sum credit accounts with a term of more than 12 months. The form and content of the annual statement is to be specified in regulations, but it is likely to include specific information detailing what has happened with the account over the previous 12 months together with some general information about debt advice and the resolution of any complaint.

A creditor would not be required to give the debtor an annual statement if there are no further sums payable under the agreement.¹¹⁷

If a creditor failed to provide an annual statement when required to do so, he would not be entitled to enforce the agreement during the period of his non-compliance and the debtor would not be liable to pay any interest during this period. Importantly, the debtor would also not be liable to pay any default sum that would have become payable during the period of non-compliance or would have become payable after the end of that period in connection with a breach of the agreement occurring during that period.¹¹⁸

b. For running account credit agreements

Clause 7 of the Bill has a similar purpose to clause 6. It inserts a new section 78(4A) into the CCA 1974, which would require creditors to issue annual statements for all regulated running-account credit agreements.

If there are two or more debtors or hirers, it would be permissible under the Bill for one debtor or hirer to provide a dispensing notice to the creditor so as to release the creditor from his obligation to provide a statement to him.¹¹⁹

2. Notice of arrears to be provided in respect of regulated credit agreements

Under the Bill the creditor will be required to send statements to the debtor more frequently if the account falls into arrears.

¹¹⁷ New section 77A(4) inserted into the CCA 1974 by clause 6 of the Bill

¹¹⁸ New section 77A(6) inserted into the CCA 1974 by clause 6 of the Bill

¹¹⁹ New section 78(4A)(3) inserted into the CCA 1974 by clause 7 of the Bill

a. For fixed-sum credit agreements

Under new section 86B, inserted into the CCA 1974 by **clause 9** of the Bill, consumer credit and hire businesses would be required to issue an arrears notice 14 days after an account goes into arrears.¹²⁰ Thereafter the credit or hire business is required to give the debtor or hirer a notice of sums in arrears at intervals of six months until:

- he ceases to be in arrears;
- has paid all sums of interest or default sums that are payable; or
- a court judgment is made in relation to the sums payable under that agreement.

Clause 9 defines arrears by reference to a failure to make a specified number of contracted repayments.¹²¹

The form and content of the arrears notice is to be prescribed by regulations but it is expected to include information about any fees and charges payable. The notice will also be required to attach an OFT information sheet on arrears, which will outline information about the options available to the debtor (for example, debt management options, time orders and contact details of debt advice providers).¹²²

b. For running account credit agreements

The Bill does not amend section 78(4) of the CCA 1974 in respect of the consumer credit business's duty to provide periodic settlements for running-account credit. It does, however, require the content of such running-account statements to include a new generic warning about the potential effect of making only minimum payments.

New section 86C, inserted into the CCA 1974 by **clause 10** of the Bill, would also provide that if a regulated running-account credit agreement falls into arrears a creditor must give the debtor a notice of sums in arrears, in the specified form, including an OFT arrears information sheet. Again, arrears are defined by reference to a failure to make a specified number of contracted repayments.¹²³ The creditor must give the notice at a time no later than the time that he is required to give the debtor the next regular statement under section 78(4) of the 1974 Act.¹²⁴ The cost of preparing and issuing the notice must be borne by the creditor (not the debtor).

¹²⁰ New section 86B is inserted into the CCA 1974 by clause 9 of the Bill

¹²¹ Provision will be made for short-term credit with high-frequency repayments

¹²² Under new section 86(A) inserted into the CCA 1974 by clause 8 of the Bill, the OFT is required to publish information sheets for debtors and hirers about arrears and default

¹²³ Provision will be made for short-term credit with high-frequency repayments

¹²⁴ New section 86(c)(2) inserted into the CCA 1974 by clause 10 of the Bill

c. Failure to give notice of sums in arrears

New section 86D, inserted into the CCA 1974 by **clause 11** of the Bill, would provide that if a consumer credit or hire business fails to give an arrears notice when required to do so in respect of a regulated fixed-sum or running-account credit agreement, the business shall not be entitled to enforce the agreement during the period of non-compliance. Specifically, it provides:

- during the period of its failure to provide the notice (i.e. from the date that it was required to be given to the date on which it is eventually provided), the business is not entitled to enforce the agreement;
- the debtor or hirer is not liable to pay any interest that relates to the period of non-compliance or to any part of it; and
- the debtor or hirer is not liable to pay any default sum which becomes payable during the period of non-compliance or where the business has failed to provide a subsequent notice to the debtor or hirer within six months of the previous notice having been provided.¹²⁵

3. Notice of default sums to be provided in respect of regulated agreements

a. Serving notice of a default sum

A ‘default sum’ for breach of the credit agreement is defined by new section 187A, inserted into the CCA 1974 by **clause 18** of the Bill:

187A (1) In this Act ‘default sum’ means, in relation to the debtor or hirer under a regulated agreement, a sum (other than a sum of interest) which is payable by him under the agreement in connection with a breach of the agreement by him.

(2) But a sum is not a default sum in relation to the debtor or hirer simply because, as a consequence of his breach of the agreement, he is required to pay it earlier than he would otherwise have had to.

By way of example, a default sum could be a charge imposed for late payment of an instalment due under the agreement or a fee imposed for exceeding a credit limit on a credit card (but it does not include interest).

Under new section 86E, inserted into the CCA 1974 by **clause 12** of the Bill, a credit or hire business must give the debtor or hirer notice within the prescribed period when a default sum becomes payable as a consequence of a breach of the agreement. The cost of preparing and issuing this notice must be borne by the credit or hire business (not the consumer).

¹²⁵ New section 86D inserted into the CCA 1974 by clause 11 of the Bill

A debtor or hirer could be required to pay interest in connection with a default sum only 28 days after the day the notice was given to him by the credit or hire business. Importantly, a credit or hire business is prevented from compounding any interest that is applied to default fees or charges; only simple interest is permitted.¹²⁶

If the creditor failed to give notice of a default sum when required to do so, the business would not be entitled to enforce the agreement during the period of non-compliance. The exact form and content of the notice may be prescribed by regulations.

b. Default notices to be amended

Currently, under sections 87 and 88 of the CCA 1974, a default notice must be served on the borrower before the credit business is entitled to take further action. **Clause 14** would amend section 88 to extend from 7 to 14 days the minimum period after which a credit or hire business may take action in respect of the agreement after having issued a default notice.

The form and content of a default notice is prescribed by the *Consumer Credit (Enforcement, Default and Termination Notices) Regulations 1983* (SI 1983/1561). **Clause 14** also amends section 88 to allow the Secretary of State to prescribe additional information in the default notice, including:

- whether there is an ‘interest after judgment’ term in the agreement (i.e. a term in the agreement that enables the consumer credit business to continue to apply interest on the debt after a judgment has been obtained);
- where the default notice is served in relation to a hire purchase or conditional sale agreement, a clear statement referring to the debtor’s or hirer’s rights under section 99 of the CCA 1974 (i.e. the right to terminate hire purchase etc agreements) and the amount that the debtor would be liable for under section 100(1) of the CCA 1974; and
- when a default notice is served on a debtor it should be accompanied with a current OFT information sheet on default.

Under **clause 17** of the Bill, consumer credit or hire businesses would be required to give notice when they are charging post-judgment interest.¹²⁷ Clause 17 provides that this notice should be given after judgment and 6 months thereafter. The notice must include information about the rate and amount of interest charged.

¹²⁶ Clause 13

¹²⁷ Clause 17 inserts new section 130A into the CCA 1974

c. Time orders

In essence, a time order is an order in which the court may reschedule any payments due under a regulated credit agreement. Under section 129 of the CCA 1974, a debtor or hirer is already entitled to apply to the court for a time order. This application can be made after having received a default notice under section 87 of the CCA 1974. However, **clause 16** of the Bill would amend section 129 to allow a debtor to seek a time order also when he first receives an arrears notice.¹²⁸ The debtor or hirer will be able to make an application only once he or she has notified the lender of his or her intention to seek a time order and made an offer for the restructuring of payments to the lender. If the debtor and lender cannot reach an agreement within 14 days, the debtor may then make an application to the court for a time order.

V Responses to the Bill

A. Consumer groups

1. General views

The majority of those consumer groups who have responded to the publication of the *Consumer Credit Bill* regard it as an important and long-overdue measure to improve consumer rights and protection.

After the Queen's Speech, both the National Consumer Council (NCC) and Citizens Advice wrote to the Prime Minister and Leader of the House of Commons urging them to give high priority and parliamentary time to the Bill.¹²⁹ Both organisations have long campaigned for reform of the CCA 1974, arguing that the current law is out of date and cannot react to the complex and burgeoning consumer credit industry. Commenting on the Bill, Jill Johnstone, NCC Director of Policy, said:

The Bill promises a new duty on lenders to treat their customers fairly and a much tougher licensing system to clamp down on bad business practice and exploitative credit agreements. It has cross-party support [...] ¹³⁰

The NCC has been particularly concerned about high interest rate charges in the doorstep collection credit market. A recent NCC report concluded that a number of characteristics of the market, including a lack of competition, are having an adverse effect on vulnerable

¹²⁸ In certain circumstances the lender or hirer is required to issue a notice of arrears by new sections 86B and 86C inserted into the CCA 1974 by clauses 9 and 10 of the Bill

¹²⁹ National Consumer Council press release, *Give consumer credit reforms top priority*, *Citizens Advice and NCC urge PM*, 9 December 2004

¹³⁰ National Consumer Council, *Give consumer credit reforms top priority*, *Citizens Advice and NCC urge PM*, 9 December 2004. http://www.ncc.org.uk/cgi-bin/kmdb10.cgi/-load384286_nccviewcurrent.htm

low-income borrowers.¹³¹ In June 2004, the NCC submitted a supercomplaint to the OFT to further investigate the UK market for home-collected credit.

Citizens Advice Bureaux (CABx) are the largest providers of free independent money advice in the UK.¹³² According to Citizens Advice, the charity representing the national network of CABx, the number of consumer debt problems dealt with by CABx has risen by nearly three quarters over the last seven years. CABx dealt with nearly 1.1 million debt-related issues in 2003. Consumer debt – which includes credit card debt, store-financed consumer purchases, car loans and personal loans – accounted for two thirds of this figure.¹³³

Citizens Advice set out its concerns about the lack of protection provided by the current consumer credit legislation in its December 2000 report *Daylight robbery: the CAB case for effective regulation of the Consumer Credit Act*.¹³⁴ It has welcomed the Bill as an important first step towards tackling extortionate credit agreements and creating a fairer consumer credit market for all consumers.¹³⁵ Specifically, Teresa Perchard, Citizens Advice Director of Policy has said:

Too many consumers have suffered for far too long for want of effective protection from the rogues and villains in the credit market. At long last the Government is calling time on credit rip-offs. The Bill offers a real chance of relief from abusive, aggressive and unfair behaviour by lenders and debt collectors. Those firms that do treat their customers fairly should not fear these much needed reforms.¹³⁶

The DTI has also quoted Teresa Perchard as saying:

We strongly support key DTI proposals to reform our outdated consumer credit laws. For too long it has been too easy to get a consumer credit licence and too hard to take them away or penalise firms for bad behaviour.

The CAB has worked closely with the DTI on the review of consumer credit legislation and is keen to see the investment in developing policy proposals come to fruition.¹³⁷

¹³¹ National Consumer Council, *Home credit: an investigation of the UK home credit market*, by Claire Whyley and Steve Brooker, June 2004, http://www.ncc.org.uk/moneymatters/home_credit.pdf

¹³² The Citizens Advice service is a network of independent charities that helps people resolve their money, legal and other problems by providing information and advice

¹³³ Citizens Advice press notice, *Citizens Advice hails consumer credit reform promised in Queens Speech*, 23 November 2004, available from: <http://www.citizensadvice.org.uk/041123>

¹³⁴ This report can be viewed on the Citizens Advice website at: www.citizensadvice.org.uk

¹³⁵ Citizens Advice press release, *Consumer Credit Bill calls time on credit cowboys, says Citizens Advice*, 16 December 2004

¹³⁶ Ibid

¹³⁷ Department of Trade and Industry press release, *Biggest shake up of consumer credit market in thirty years*, 16 December 2004

Which? (formerly the Consumers' Association) is said to support the Bill because it should give consumers greater protection against unfair lending.¹³⁸ However, it is calling for a number of other measures including: credit cards to have only one way of allocating interest so that people can better compare rates; sharing of customers' full credit history between lenders to ensure responsible lending; and banning the automatic inclusion of Payment Protection Insurance in credit quotes which can increase the cost of the loan without customers realising.¹³⁹

2. A cap on interest rates?

During the three-year review of the consumer credit laws, some consumer groups have called for a ceiling to be imposed on lenders' interest rates.¹⁴⁰ In response, the Government has stated that, for various reasons, it is not persuaded that this is the right course of action:

It has been suggested by some consumer groups that one mechanism for controlling the cost of credit is to limit the rate of interest charged. The overwhelming advantage claimed for this mechanism is its simplicity. Several other EU Member States and some of the states in the United States of America have ceilings. The UK, itself, had what was, in effect, a ceiling prior to the introduction of the CCA. The Moneylenders Acts provided that a rate in excess of 48% was prima facie excessive and the transaction harsh and unconscionable. However, the Crowther Committee concluded that, in practice, the protection accorded was largely ineffective.¹⁴¹

The Government is not yet persuaded that the introduction of an interest rate ceiling for the UK is the right approach to provide protection from excessive credit costs. While the Government acknowledges that there are some benefits from having a clear and simple-to-administer system, there are a number of problems associated with interest rate ceilings:

- The UK has a sophisticated and diverse credit market. There would be many practical difficulties in introducing a capping regime that would apply to so many different types of credit arrangement.
- A high APR is not necessarily indicative of an extortionate or high-cost loan. For example, the amount of interest repayable for very short-term loans may appear relatively modest, and yet can result in a very high APR.

¹³⁸ *Queen's Speech – Key Plans*, ePolitix, 23 November 2004:
<http://www.epolitix.com/EN/ForumBriefs/200411/e2b92153-7ada-45d9-bce1-7610fe9d938d.htm>

¹³⁹ Ibid

¹⁴⁰ <http://www.which.net/campaigns/personalfinance/credit/creditact.html>

¹⁴¹ *Consumer Credit*, Cmnd 4596, Report of the Committee, Lord Crowther, 1971, (s) 6.6.3 – 6.6.4

- Creditors could manipulate the APR by extending the minimum term over which credit can be taken. This would result in the APR being reduced, although the total interest repayable might actually increase.
- If creditors are required to reduce their rates to come within a rate ceiling, they could make the cost of credit to consumers more expensive in other ways. For example, many weekly doorstep lenders do not, at present, charge for missed or late payments, but could decide to introduce such charges.
- Rate ceilings could actually have the effect of encouraging rates to gravitate towards that ceiling.
- A rate ceiling may also result in some lenders withdrawing from the market. This, in turn, may lead to groups of consumers being denied ready access to alternative forms of credit, forcing them to resort to illegal moneylenders.
- EU Member States who have rate ceilings, tend to have a less diverse credit market.

Therefore, the Government is not yet persuaded of the case for interest rate ceilings.¹⁴²

The Government's decision not to impose a cap on interest rates has, in part, been informed by independent research it commissioned on the effect of interest rate controls in France, Germany and the USA.¹⁴³ However, the Government has said that it will keep the option of interest rate controls under review.¹⁴⁴

B. Business groups

Those business groups who have responded are broadly in favour of the Bill. The British Bankers Association (BBA) has welcomed the Bill saying that the timing was right and the way it had been drafted seemed sensible. Ian Mullen, Chief Executive of the BBA said:

The existing Consumer Credit Act has served us well, but it is 30 years old and the consumer credit environment has changed dramatically during that period. The time is now right to review it.

¹⁴² Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

¹⁴³ Department of Trade and Industry, “*The effect of interest rate controls in other countries*”, by Policis (an independent company on behalf of the DTI), 26 August 2004:

¹⁴⁴ Department of Trade and Industry, *Questions and Answers on the Consumer Credit Bill*, December 2004: <http://www.dti.gov.uk/ccp/creditbill/pdfs/creditbillqa.pdf>

The DTI press release suggests that the Government is making broadly sensible changes. The Government clearly wishes to crack down on rogue lenders – a move which responsible lenders such as banks welcome. Banks' customers have been able to refer unresolved complaints to an Ombudsman for over a decade and it is appropriate that the same right will now apply to all credit agreements.

The provisions in this Bill likely to apply to customers in financial difficulty would appear to support actions which banks have in place to ensure that help is available for this minority of customers.

We will of course be looking very carefully at the detail of the Bill in the coming days, and looking to continue working closely with the DTI as it presses through its Parliamentary stages.¹⁴⁵

The Association for Payment Clearing Services (APACS) also welcomed the Bill. Sandra Quinn, director of corporate communications for APACS, is reported to have said:

We are pleased to see the Consumer Credit Bill in the Queen's Speech. It will add to efforts on the part of the industry already underway to make the credit market more transparent.

From what we understand the Bill is working very much with the grain of the changes in the latest draft of the Banking Code which includes the summary boxes, clearer marketing practices and warnings about over indebtedness for which the government are likely to be legislating.

This is the second stage of changes coming out of the government's review of the 1974 Consumer Credit Act – the industry has already agreed to a range of changes in partnership with the government such as a single APR calculation and alterations to the form and content of credit agreements.

The industry also welcomes the expected measures to crackdown on predatory lending by loan sharks. People deserve protection from some of the appalling practices seen in this unregulated market.

Credit cards remain one of our most popular payment tools in the UK, with more than 30 million customers. This is one of the world's most competitive markets. The industry hopes that the Bill will further strengthen the credit card market.¹⁴⁶

The Association of Chartered Certified Accountants is also said to support the Bill on the basis that with consumer debt so high in the UK, resulting in an increasing number of bankruptcies, consumers need additional protection against unfair credit practices.¹⁴⁷

¹⁴⁵ British Bankers' Association press release, *BBA response to Consumer Credit Bill*, 16 December 2004

¹⁴⁶ *Queen's Speech – Key Plans*, ePolitix, 23 November 2004:
<http://www.epolitix.com/EN/ForumBriefs/200411/e2b92153-7ada-45d9-bce1-7610fe9d938d.htm>

¹⁴⁷ Lenders seek to limit impact of *Consumer Credit Bill*, Financial Times, 24 November 2004

It is reported that some lenders are concerned that the drafting of the proposed unfair credit test, which will apply throughout the lifetime of a credit agreement, could allow borrowers to challenge mainstream products charging unexceptional interest rates.¹⁴⁸ There is concern that the Bill's "open-ended unfair lending test and the ADR system could become a troublemaker's charter, which in turn could lead lenders to be overly cautious".¹⁴⁹ The BAA is reportedly looking for a clean and simple test of how fairness in a credit agreement would be judged by the court.¹⁵⁰ Some lenders also remain concerned about the abolition of the £25,000 financial limit exposing them to greater liability.

The Confederation of British Industry (CBI) has accepted the need to update existing credit legislation but has stressed that the reform must be workable in practice. It has called for the provisions of the Bill be properly defined and without unintended consequences.¹⁵¹

Although the Finance and Leasing Association (FLA) supports many of the proposals outlined in the DTI's consumer credit White Paper, *Fair, Clear and competitive: the Consumer Credit Market in the 21st Century*, it has expressed concern that some proposals may have unintended consequences and may hit hardest those in most need of the benefit of reforms to the CCA 1974:

We completely support targeted measures aimed at promoting a competitive, transparent and responsive credit market, built on responsible lending. We are, however, concerned that the proposals could easily backfire, increasing the cost of credit and creating credit deserts for consumers with little or no access to the mainstream market. There is a real threat that many of the poorest people – those who need affordable credit most – could be worst hit.

The White Paper sets out a radical agenda to update and increase the protection afforded by the UK's consumer credit laws. Key focus areas, with which we agree, include fostering greater transparency in consumer finance, reducing red tape for credit adverts and improving financial literacy. We further hope that it will also be possible to reduce the red tape applying to the form and content of credit agreements, multiple agreements and modifying agreements.¹⁵²

Responding to the White Paper, the FLA highlighted a number of specific concerns including:

¹⁴⁸ Ibid

¹⁴⁹ Ibid

¹⁵⁰ Ibid

¹⁵¹ Ibid

¹⁵² Finance and Leasing Association, *FLA's response to DTI's Consumer Credit White Paper, Fair, Clear and Competitive: The Consumer Credit Market in the 21st Century*, 15 March 2004, available at: http://www.fla.org.uk/fla_home/Consultation_Papers/CCA%20WHITE%20PAPER.doc

Timetable – this is now very tight and may mean that plans are rushed through, giving lenders an impossible time frame in which to make changes.

Retrospection – of early settlement changes and the unfair lending proposals (replacing “extortionate credit”) to existing loans could mean that existing credit contracts could be challenged under the new measures. This poses a particular threat to securitisation and entry of new lenders to the market.

Removal of the financial limit – whilst we welcome the proposals to retain the limit for business lending and believe a workable mechanism can be developed to distinguish between business and consumer borrowing, we are concerned that the abolition of the limit for consumer lending will cause unwarranted costs, particularly in the context of voluntary terminations.

Credit agreements – Whilst the intended benefits of clearer information are, at face value, attractive and have our full support, we believe that the proposals set out in the White Paper and the Consultation Document will not achieve the desired aim and are unacceptable as they stand. Our detailed observations in this respect are set out in our response to the Consultation Document.

Distortion of competition - the proposals will impact on different types of lenders and products unevenly. As an illustration, lenders offering multiple products through multiple channels (i.e. branch, telephone, internet, broker and third-party retailers) will have significantly more changes to make implementing the proposals than monoline lenders, or lenders offering one product in multiple markets.

Micro-regulation – detailed legislative rules could stifle innovation and undermine the flexibility provided in this area by industry codes of practice.¹⁵³

Responding to a previous DTI consultation document on the introduction of an ADR scheme, the FLA gave a number of reasons as to why it was not in favour of referring complaints immediately to a formal ADR provider:

We, and our members, regard our complaints handling scheme as playing an important role in resolving consumer credit disputes. Consequently, we see no benefit in referring each and every consumer credit complaint directly to an Ombudsman or arbitrator, particularly one with a charging structure comparable to that of FOS. First, conciliation is an important step in the complaint resolution process. Secondly, the immediate reference of complaints to a formal ADR provider would have a directly negative cost impact upon our members, which would inevitably have a knock on effect to consumers. And finally, we believe that we can offer added value to the consumer by way of our favourable complaint resolution time (...) and the personalised service we offer. Moreover, the data we obtain in the course of operating the scheme gives us a strong feel as

¹⁵³ Ibid

to how our code of practice (the Lending Code) is functioning and is how we ensure the Code remains relevant to the industry. It helps us monitor the effectiveness of members' complaints handling. Loss of this intelligence would severely hamper the development of our Code and would be a retrograde step.¹⁵⁴

Despite these reservations, the FLA generally welcomes the Bill. Commenting directly on the Bill, Martin Hall, Director General of FLA, has said:

Last December's Consumer Credit White Paper set out a radical agenda to review the UK's outdated consumer credit laws. It also recognised the vital contribution the credit industry makes to the UK economy. We are hoping the Bill successfully captures this approach.

FLA will continue to support targeted measures which genuinely promote competitive, transparent and responsive markets, built on responsible lending. We shall scrutinise the Bill to make sure it doesn't have unintended consequences.¹⁵⁵

However, the FLA has also confirmed its intention to press for further reform of hire purchase law:

The new Bill proposes wholesale reform of consumer credit legislation. It will give the opportunity to update key parts of the existing law in line with modern markets, modern consumers and modern business practices. The FLA would like to see changes to the law which promote a fair balanced and competitive market place which benefits both consumers and businesses. As part of this approach we will also be pressing the DTI for further reform of the out-of-date hire purchase law.¹⁵⁶

The British Vehicle Rental and Leasing Association (BVRLA) is the representative trade body for companies engaged in leasing cars and commercial vehicles. It has also responded cautiously to the proposals contained in the White Paper:

It is clear that a small minority of lenders are causing the majority of the 'socially harmful lending' to consumers. As a business representative body of the family of good lenders, we support a pragmatic 'root and branch' approach to effectively remove such lending practices.

The DTI is nevertheless encouraged to utilise this review by implementing only the justifiable and necessary changes as identified and proven. In particular, a

¹⁵⁴ Finance and Leasing Association, *FLA's response to DTI's Consultation Document on the Provision of Alternative Dispute Resolution for Disputes Arising under the Consumer Credit Act 1974*, 16 March 2004, available at:

http://www.fla.org.uk/fla_home/Consultation_Papers/Responses%20to%20ADR%20Consultation.doc

¹⁵⁵ Finance and Leasing Association, *Credit Industry Response to Biggest Shake Up of Consumer Credit Market in Thirty Years*, 16 December 2004

¹⁵⁶ Ibid

targeted and proportionate approach should be adhered to when attempting to protect the most vulnerable consumers to help ensure that an unnecessary burden is not imposed on legitimate lenders. Ultimately, we remain concerned with the unintended consequences of the proposals, which could have an undesired effect of damaging the credit market, and increase the cost of lending, which will have an adverse impact on the most vulnerable sector of society.

[...] With the development of an innovative consumer credit market over the past 30 years, the key aims and objectives as outlined in the White Paper are clear. However, these proposals must be translated appropriately and the DTI must ensure that it meets the new challenges of the credit market in a positive and fair manner.¹⁵⁷

C. Small businesses

Under the provisions of the Bill, the CCA 1974 is able to regulate business lending only on loans of up to £25,000 to small businesses (meaning sole traders, unincorporated associations and partnerships of three or fewer members). The Federation of Small Businesses (FSB) has expressed its disappointment that the Bill does not go further. The FSB argues that the Bill should be extended to cover all lending to small businesses:

Small businesses need similar protection afforded to consumers as entrepreneurs often use their house for security and lack specialist financial knowledge.¹⁵⁸

A spokesman for the FSB is also reported to have said:

It tends to be the case that small businesses get tied into contracts that are more onerous than those for individuals. Although we haven't seen any particular examples of small businesses being targeted by credit scams, it is happening in other areas.¹⁵⁹

Commenting on its reasons for not extending the protection of the CCA 1974 to small businesses loans in excess of £25,000, the Government has said:

Removal of the financial limit would mean that all business lending to partnerships and sole traders would be caught by the CCA. This would be likely to result in the cost and access to high-value finance for small businesses being adversely affected in the following ways:

¹⁵⁷ British Vehicle Rental and Leasing Association, *Fair, Clear and Competitive: The consumer credit market in the 21st century – response from BVRLA*, March 2004

¹⁵⁸ Federation of Small Businesses press release P2004/55, *FSB applauds departments with few bills to their name – small business reaction to Queen's speech*, 23 November 2004, <http://www.fsb.org.uk/news.asp?REC=2212>

¹⁵⁹ Ibid

- The CCA contains a provision that allows Hire Purchase (HP) agreements to be voluntarily terminated and the goods handed back if a minimum of one half of the total sums due have been paid back. While this is relatively manageable for lower value goods, removal of the financial limit would expose HP providers of, often, bespoke equipment, to returned goods, which may then be of little or no re-sale value. Estimates suggest that in excess of 70% of business lending on HP terms is for specialist equipment above £25,000 and, therefore, currently unregulated. This represents a considerable risk to the credit provider.
- The existence of cooling-off protections for agreements concluded away from trade premises could restrict the flexibility of business lending and the speed of access to finance. Concluding business transactions in this manner is common practice and such delays may result in the skewing of business lending to other forms of borrowing, which are neither regulated nor appropriate.

Following extensive consultation, the Government believes that some business lending below £25,000 should still be regulated to protect the most vulnerable business borrowers who do not have access to mainstream lenders.

[...] The £25,000 limit continues to be appropriate for this purpose as it provides a reasonable upper limit for vulnerable businesses. Borrowing above this figure is likely to be secured by a charge over the assets being purchased, which will entail both a higher level of advice (including legal advice), and recourse to the underlying assets.

Retention of the limit provides suitable protection for the vulnerable, small businesses but, importantly, also facilitates ease and speed of access to vital business funding above £25,000, where its use is solely for business purposes.¹⁶⁰

D. Office of Fair Trading

Unsurprisingly, Government plans to modernise consumer credit law, have been welcomed by the OFT. The OFT has long called for reform to the existing CCA 1974, arguing that it is now outdated. John Vickers, OFT Chairman, has said:

Reform is necessary to ensure that credit regulation is relevant to today's growing market, enabling more effective regulation of the credit industry and greater consumer protection.¹⁶¹

¹⁶⁰ Department of Trade and Industry White Paper, *Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century*, Cm 6040, 8 December 2003

¹⁶¹ Office of Fair Trading press release 210/04, *OFT welcomes consumer credit bill*, 16 December 2004

In its response to the DTI's consultation on credit licensing, the OFT agreed that a wider range of penalties and other reforms are needed to ensure more effective regulation of the credit industry.¹⁶² Penny Boys, OFT Executive Director, said:

Consumers need protection in the market for credit, which can be a high-risk product and can be complex and difficult to understand. The licensing system should allow the OFT to screen out unfit traders and target regulatory action where it is needed, without imposing unnecessary burdens on business.¹⁶³

VI Further Reading

1. The *Consumer Credit Bill* [Bill 16] and its explanatory notes [Bill 16-EN] are available from the UK Parliament website:
<http://www.publications.parliament.uk/pa/cm200405/cmbills/016/2005016.htm>
2. HM Treasury, *Promoting financial inclusion*, December 2004.
<http://www.dti.gov.uk/ccp/topics1/pdf1/creditpolicis1.pdf>
3. Department of Trade and Industry, *The effect of interest rate controls in other countries*, report by Policis, 26 August 2004.
<http://www.dti.gov.uk/ccp/topics1/pdf1/creditpolicis1.pdf>
4. Department of Trade and Industry and Department for Work and Pensions, *Tackling Over-Indebtedness Action Plan 2004*, July 2004.
<http://www.dti.gov.uk/ccp/topics1/pdf1/creditpolicis1.pdf>
5. Finance and Leasing Association, *Monthly Statistics*, July 2004.
<http://www.fla.org.uk/>
6. Department for Work & Pensions, *Characteristics of families in debt and the nature of indebtedness*, Kempson, McKay and Willetts, June 2004.
<http://www.dwp.gov.uk/asd/asd5/rports2003-2004/rrep211.asp>
7. National Consumer Council, *Home credit: an investigation of the UK home credit market*, by Claire Whyley and Steve Brooker, June 2004.
http://www.ncc.org.uk/moneymatters/home_credit.pdf
8. Department of Trade and Industry, *Qualitative research into consumer understanding of the form and content of credit product documents*, a report for the DTI by MORI Financial Services and Front Line Research, April 2004.
<http://www.dti.gov.uk/ccp/topics1/pdf1/creditreport0505041.pdf>

¹⁶² Department of Trade and Industry, *Consumer Credit Licensing – A consultation document on the licensing regime of the Consumer Credit Act 1974*, 30 January 2003

¹⁶³ Office of Fair Trading press notice PN 55/03, *OFT welcomes plans to strengthen credit licensing laws*, 8 May 2003

9. Office of Fair Trading, *Debt consolidation: A report on an OFT study*, March 2004.
<http://www.offt.gov.uk/NR/rdonlyres/D83F41F8-A747-4CA3-8217-24195CD594CC/0/oft705.pdf>
10. Department of Trade and Industry, *Fair, Clear and Competitive – The consumer credit market in the 21st century*, Cm 6040, December 2003.
<http://www.dti.gov.uk/ccp/topics1/pdf1/creditwp.pdf>
11. Citizens Advice, *In too deep, CAB clients' experience of debt*, Sue Edwards, May 2003. <http://www.citizensadvice.org.uk/in-too-deep.pdf>
12. Department of Trade and Industry, *Over-Indebtedness in Britain: A report to the Department of Trade and Industry*, Elaine Kempson, 2002.
<http://www.dti.gov.uk/ccp/topics1/overindebtedness.htm>
13. Department of Trade and Industry, *Review of the Consumer Credit Act – progress report*, August 2002 (URN 02/1241).
14. *Report by the Task Force on Tackling Overindebtedness*, July 2001 (URN 01/1019).
15. Financial Services Authority, *In or Out? Financial Exclusion: a literature and research review*, Kempson, Whyley, Caskey and Collard, July 2000.
<http://www.fsa.gov.uk/pubs/consumer-research/crpr03.pdf>
16. Office of Fair Trading survey, *Consumer Detriment*, April 2000.
<http://www.offt.gov.uk/NR/rdonlyres/DC30AD21-35C5-4881-9E60-AEDF52B9D4D5/0/oft296.pdf>
17. National Association of Citizens Advice Bureaux, *Daylight Robbery - The CAB case for effective regulation of extortionate credit*, December 2000.
http://www.citizensadvice.org.uk/pdf_drob.pdf
18. HM Treasury, *Access to Financial Services*, 1999.
19. Department of Trade and Industry, *Extortionate Credit in the UK*, Elaine Kempson and Claire Whyley, June 1999.
<http://www.dti.gov.uk/ccp/topics1/extortionate.htm>
20. Office of Fair Trading, *Unjust credit transactions – a report by the Director General of Fair Trading (Sir Gordon Borrie QC) on sections 137-140 of the Consumer Credit Act 1974*, OFT 046, 1991.
21. Crowther Committee: *Consumer Credit – Report of the Committee*, Cmnd 4596, March 1971.
22. British Standards Institute, *Consumer Effectiveness Project*, available at:
<http://www.bsi-global.com/All+About+Stanards/Consumers/research.xalter>

23. Further information about the Government's Over-Indebtedness Strategy can be viewed on the DTI website at:

<http://www.dti.gov.uk/ccp/topics1/overindebtedness.htm>

24. Information about the OFT's credit campaign can be viewed at:

<http://www.ofi.gov.uk/Consumer/Credit/default.htm>

Appendix: Consultations

The DTI has undertaken the following formal consultation exercises as part of its review of the UK consumer credit laws:

1. DTI, *Tackling Loan Sharks and More! Modernising the Consumer Credit Act 1974*, July 2001, (CA 005/01) (URN 01/1057):

<http://www.dti.gov.uk/ccp/consultpdf/loanshark.htm#intro>

This document considered the effectiveness of the CCA 1974 and priorities for reform. The consultation period ended on 3 October 2001 with the DTI receiving 107 responses.

2. DTI, *Consultation document on the financial limit and exempt agreements of the Consumer Credit Act 1974*, (CA 005/002), March 2002, (URN 02/857):

<http://www2.dti.gov.uk/ccp/consultpdf/loanshark2.pdf>

This document considered removing the £25,000 financial limit in the CCA 1974 and reviewing the status of some exempt agreements. The consultation period ended on 21 June 2002 with the DTI receiving 55 responses. A summary of responses to this consultation was published in November 2002:

<http://www2.dti.gov.uk/ccp/consultpdf/finlimitssumm.pdf>

3. DTI, *Consultation document on the early settlement of consumer credit agreements under the Consumer Credit Act 1974*, August 2002, (CCP 02/02) (URN 02/1240): <http://www.dti.gov.uk/ccp/topics1/pdf1/earlycredit.pdf>

This consultation period ended on 22 November 2002 with the DTI receiving 38 responses.

4. DTI, *Consultation document on enabling and facilitating the conclusion of credit and hire agreements electronically under the CCA 1974*, December 2002, (CCP 015/02): <http://www.dti.gov.uk/ccp/consultpdf/eagree.pdf>

The consultation period ended on 28 March 2003 with the DTI receiving 35 responses.

5. DTI, *A consultation document on the licensing regime under the Consumer Credit Act 1974*, January 2003 (CCP 005/03) (URN 03/627):

<http://www.dti.gov.uk/ccp/consultpdf/credlic.pdf>

The consultation period ended on 30 April 2003 with the DTI receiving 57 responses.

6. DTI, *Tackling Loan Sharks and More!* (CCP 007/03), March 2003, (URN 03/726): <http://www.dti.gov.uk/ccp/consultpdf/extortcon.pdf>. This consultation document considered proposals for reform of the protections offered to consumers in respect of extortionate credit. The consultation period ended on 6 June 2003 with the DTI receiving 70 responses.
7. DTI, *Establishing a Transparent Market: A consultation on proposals for regulations on: early settlement, consumer credit advertising, form and content of credit agreements, APRs on credit cards, on-line agreements*, 8 December 2003: <http://www.dti.gov.uk/ccp/topics1/pdf1/creditpiu.pdf> A summary of responses is available at: <http://www.dti.gov.uk/ccp/topics1/pdf1/creditconres.pdf>
8. DTI, *Consultation document on the Provision of Alternative Dispute Resolution (ADR) for disputes arising under the Consumer Credit Act 1974*, 17 December 2003: <http://www.dti.gov.uk/ccp/consultpdf/adrcondoc.pdf> The consultation period ended on 14 March 2004 and a summary of responses has been published: <http://www.dti.gov.uk/ccp/topics1/pdf1/creditadrconresp.pdf>

In addition, the DTI has published two White Papers:

1. DTI White Paper, *Modern Markets: Confident Consumers*, Cm 4410, 22 July 1999: <http://www.dti.gov.uk/consumer/whitepaper/wpmenu.htm>
2. DTI White Paper, *Fair, Clear and Competitive – the Consumer Credit Market in the 21st Century*, Cm 6040, December 2003: <http://www.dti.gov.uk/ccp/topics1/pdf1/creditwp.pdf>