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## High cost consumer credit – scope and reasons for a review

2 July 2009

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### Summary

1. Following our announcement on 7 April 2009 of plans to launch a review into the consumer credit sector as part of our wider Financial Services Strategy, we have received a significant number of submissions from interested parties commenting on the scope of the review we had proposed.
2. Taking account of the initiatives and other changes which are already underway in this sector, the review will focus on the high cost area of the sector, where APRs are high, and where consumers may have an urgent need of credit, be more vulnerable and face a smaller number of products to choose from. The current recession is also likely to increase the number of consumers seeking high-cost credit and the potential for consumer detriment.
3. The review will focus on high cost credit to assess the effectiveness of competition; examine suppliers' offerings; and improve our understanding of consumer behaviour and decision-making. We will assess the current level of competition and understand whether suppliers are able to, and do, compete vigorously to deliver benefits for consumers. We will also assess whether consumers have the appropriate level of protection and receive the information they need to allow them to make informed and well judged decisions about high cost credit products.

## **Timing of the review**

4. The turbulence in global financial markets has brought about changes in both the availability and cost of consumer credit. It is appropriate for the OFT to undertake a review of high cost credit at this time to establish the impact these changes have had on the sector and consumers.
5. We are aware that there is considerable work currently underway in the broader consumer credit sector including work on the implementation of the Consumer Credit Directive from 2010, the OFT's project to provide guidance on irresponsible lending, and a number of Government initiatives in relation to debt collection and advice.
6. We have had regard to these initiatives when considering both the scope and timing of the review. Delaying the review would risk losing the opportunity to gain an understanding of the current state of the high cost credit sector and using this to inform our regulatory stance. Carrying out the review now would, however, risk placing an information burden on stakeholders additional to that arising from the work already underway in, or planned for, the sector.
7. We have taken the decision to proceed with the review to improve our understanding of the changes to the sector while they are current and to inform our regulatory stance. In doing so, we have sought to limit the information gathering burden on stakeholders to the minimum necessary to secure the review's aims.

## **The scope and focus of the study**

8. We have reassessed the scope of the review in light of the consultation responses we received and the work that is either currently underway or due to be started in the credit sector. We have narrowed the scope of the review to high cost credit. This will avoid duplication with other initiatives, refine our focus to an area where we consider consumers are most vulnerable and where the OFT can add most value, and reduce the information burden on stakeholders.

## **Informal consultation on the scope of the review**

9. We received over 20 responses to our informal one month consultation on the scope of the review of consumer credit. There was a broad range of responses, including views which considered that the scope was too narrowly drawn, some considering it to be too broad, and many responses considered the scope to be appropriate. One of the most common requests was to expand the scope to include debt recovery issues and claims management firms. A number of responses were unsure of the reasoning for the review and the benefits that it might bring for the industry.
10. In this document we have sought to respond to the questions raised in the informal consultation by seeking to explain more fully the revised scope of the review, the reasoning behind this work and the benefits that we envisage for consumers and fair-dealing businesses.
11. Further details of the nature of the comments received in response to the informal consultation can be found on the high cost credit review pages of the OFT website.

## **The focus of our work**

12. This will be an evidence-based review looking at the overall operation of and interaction between the different elements of the high cost credit sector. We will consider the implications for competition among suppliers of products and between different products in the sector and the implications for consumers, consumer protection and effective consumer decision-making.
13. We have identified four areas on which we will focus. These are:
  - **Understanding consumer behaviour.** We intend to examine the following elements of consumer behaviour in relation to credit generally and specifically to high cost credit:
    - **Understanding of features and products** – we are interested in the level of consumer understanding of credit products and

their key features. This research will be useful for considering the effectiveness of future regulatory changes, consumer information and education campaigns and enforcement work by OFT.

- **Factors affecting choices** – we are interested in the factors on which consumers base their decisions about the type of product and supplier they select. This will help determine the dimensions of competition in the sector and consideration of the absolute level of competition faced by firms. It is also useful in observing the elements which consumers find to be most persuasive in particular products.
- **Constraints on choices** – we are aware that there are a number of factors that limit the extent of the choices consumers are able to make in practice. Understanding these will give us a greater insight into the level of competition seen by consumers, as well as the potential for interaction between consumers' current and future credit commitments.
- **Understanding lender dynamics.** There are two elements to our work in this area:
  - **Understanding the business models and implications of these for competition in the market(s)** – this includes considering the different sources of revenue for suppliers and their relative significance, as well as the extent to which these are visible and can be assessed and compared by consumers.
  - **Understanding the impact of the global turbulence on suppliers and competition in the market(s)** – we wish to understand the impact of the turbulence in global financial markets on providers of high cost credit and the implications this has for competition, the availability of credit and the vulnerability of consumers.
- **Considering relevant practices in other countries.** We intend to consider the extent of similarities and differences between the UK

and a number of other countries in relation to credit generally and specifically for high cost credit. This will allow for the comparison of approach, regulation, competition and efficiency between such countries and the UK.

- **Quantification of any consumer detriment found in relation to high cost credit and the development of appropriate remedies where necessary.** One part of this work is to consider whether competition is working effectively to the benefit of fair-dealing businesses and consumers, or whether they are suffering some degree of detriment from a lack of competition or other practices. Where a significant level of detriment is seen, we may consider whether it is appropriate for the OFT to make recommendations to the Government to resolve any matters of concern or take our own enforcement action.

14. The review will consider products available to relatively high risk and/or low income and vulnerable consumers. We will examine both secured and unsecured credit products where they fall within the scope of high cost consumer credit.
15. In addition, we intend to examine what lies behind the decision to take out a new credit product or agreement. This will allow us to consider both the extent of competition in the sector and the appropriate way in which to assist consumers in making effective decisions.

### **A key part of the Financial Services Strategy**

16. This review is an important part of the OFT's Financial Services Strategy. The review is a clear part of the promotion of fairness and responsibility in relation to high cost credit, where consumers are likely to be more vulnerable.
17. The review of high cost credit fits with both the short term and longer term objectives of the draft Financial Services Strategy. In addition, the Strategy notes that the credit sector is one where the impact of the global financial turbulence will be relatively significant. Our focus on the high cost element of the credit sector ensures that we will address

potential concerns about the most vulnerable of consumers and the element of the sector most significantly affected in the recession.

**Complements the work of the Department for Business Innovation and Skills (BIS) outlined in its Consumer White Paper**

18. BIS has published its Consumer White Paper today. This contains proposals on real help for vulnerable consumers; a new approach to personal finance; empowering consumers through better enforcement and information and modernising consumer law.
19. Narrowing the scope of the review to cover high cost credit, where consumers are likely to be more vulnerable, ensures it remains consistent with BIS' aims to assist this group of consumers. We maintained a dialogue with BIS during our scope-development work and this has ensured that the review's scope is complementary to and does not overlap with the proposals BIS has announced.

**Issues which are outside the OFT's focus or remit**

20. Our review is limited to considering the nature and extent of competition in the high cost credit sector and the levels of consumer protection that would allow consumers to make informed and well judged decisions in relation to high cost credit products.
21. We do not intend to consider first-charge mortgages within the scope of this review; however, we will consider second charge mortgages, where they compete with specific unsecured high cost credit products.
22. We will not address debt collection within the review. While this is a significant concern in relation to the consumer credit sector as a whole, and was noted as such by a number of stakeholder responses to our informal consultation, there is considerable government work already underway in this area to address these concerns.

## Timetable and process of the review

### Indicative timescale

23. Following today's launch, we expect to publish our interim findings by the end of 2009, with the final report to be available in Spring 2010.

### Contacting the OFT

24. We propose to conduct this review by gathering and analysing information provided by businesses, industry associations, consumer organisations, central government, and independent experts, through submissions, meetings and questionnaires. We envisage that the co-operation of these interested parties will enable us quickly to obtain the limited information and evidence that we require for the review.
25. We will be contacting specific bodies directly seeking specific information and evidence to allow us to reach appropriate conclusions on the operation of, competition and consumer protection in the consumer credit sector.
26. In addition to any direct contact, we welcome relevant submissions on this review. Submissions should be sent to:

High Cost Credit Review (c/o Peter Hill)  
Fourth Floor  
Office of Fair Trading  
Fleetbank House  
2-6 Salisbury Square  
London EC4Y 8JX

Alternatively they can be emailed to: [creditreview@oft.gsi.gov.uk](mailto:creditreview@oft.gsi.gov.uk)

27. It will assist the case team if submissions are laid out as follows:
- A summary of the main points you would like the OFT to consider.

- A more detailed explanation of these points and how they relate specifically to the scope of the review.
  - Evidence to support the views being made:
    - if this includes data or financial figures, precise definitions, the dates and source of the data should be provided
    - if this includes detailed calculations, an annexe or spreadsheet which allows the OFT to replicate these calculations should be provided
    - if this includes specific examples of events, a chronology and background to the events should be provided
    - if this includes comparators, the reasons why you consider the comparator to be appropriate should be provided
    - if you are willing to answer questions further to your submission, a named point of contact and contact details including telephone number, whom the review team can contact should be provided.
  - Please indicate any specific parts of the submission that you consider to be confidential and your reasoning for your assessment.
  - If the submission is representing a business:
    - the company name and ultimate ownership
    - a brief summary of the activities of the company
28. Please note that information provided to the OFT may be the subject of requests from the public for information under the Freedom of Information Act 2000. In considering such requests for information we will take full account of any reasons provided by respondents in support of confidentiality, the Data Protection Act 1998 and our obligations under Part 9 of the Enterprise Act 2002.
29. We recognise that it is not always possible to provide complete evidence to support views. We would however be interested in suggestions for sources of data to support views that we could

consider. However, we may not be in a position to pursue all avenues in this review. Where no evidence is provided, the weight we can place on the views is lower than where evidence is provided.

**30. The deadline for receiving responses is 28 August 2009.**

31. Contact details for the team are as follows:

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