

Report of Assistant Chief Executive (Citizens and Communities)

Report to Executive Board

Date: 17th September 2014

Subject: Regulation of the High Cost Short Term Credit Market by the Financial Conduct Authority

Are specific electoral Wards affected? If relevant, name(s) of Ward(s):	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Are there implications for equality and diversity and cohesion and integration?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Is the decision eligible for Call-In?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Does the report contain confidential or exempt information? If relevant, Access to Information Procedure Rule number: Appendix number:	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No

Summary of main issues

1. At the meeting of Executive Board on 16th July 2014 a request was made that a report be submitted to its next meeting regarding the proposals by the Financial Conduct Authority (FCA) regarding a price cap on High Cost Short Term Credit.
2. As of 1st April 2014, the Financial Conduct Authority took over the regulation of around 50,000 consumer credit firms from the Office of Fair Trading (OFT). From July 2014 the FCA implemented their rules for consumer credit firms, setting out higher standards for payday and other high-cost short-term lenders and for debt management firms. This includes limiting the number of times a loan can be 'rolled over' and the number of unsuccessfully attempts for collection, as well as reviewing how borrowers are treated if they are unable to repay.
3. In November 2013 the government placed a legal duty on the FCA to impose a total cap on the cost of high cost short term credit, to be in place no later than 2nd January 2015. In July 2014, the FCA published their proposals for a consultation on the level at which the cap will be set.
4. Leeds City Council submitted a response to the FCA consultation. Overall, the response supported the proposed structure of the cap and the fact that the cap covers the total cost of credit in order to prevent lenders from charging

excessive fees. However, concern was expressed around the level of the cap, which appears to be geared towards ensuring the High Cost Short Term Credit (HCSTC) sector continues to operate rather than concentrating primarily on consumer protection.

Recommendations

5. Executive Board is asked to note the content of this report and in particular Leeds City Council's response to the FCA consultation set out in Appendix 1.
6. The Chief Executive is asked to write to all Leeds MPs, asking them to consider Leeds City Council's response to the FCA consultation as set out in appendix one and to urge them to take up the issues raised within the Council's response.

1 Purpose of this report

- 1.1 To provide the Executive Board with details of the actions the FCA has taken to regulate the High Cost Short Term Credit (HCSTC) industry since 1st April 2014, and details of their consultation on the proposed cap on the total cost of high cost credit.

2 Background information

- 2.1 At the meeting of Executive Board on 16th July 2014 a request was made that a report be submitted to the September meeting regarding the proposals recently announced by the FCA regarding a price cap on HCSTC.
- 2.2 The HCSTC market is comprised of home credit, pawn brokers, money shops, payday lenders and rent to buy shops. The type of finance offered is typically; unsecured, low value (average loan £260), short term (typical loan period 30 days), and high cost (average cost 25% per month).
- 2.3 The HCSTC industry has been thriving in recent years. The OFT estimated that the value of the payday lending market increased by 60% between 2008 and 2012, from £900 million to an estimated £2.2 billion. According to recent data obtained by the FCA, in 2013, 1.6 million customers took out 10 million loans, with a total value of £2.5 billion.
- 2.4 In their Compliance Review of the Payday Lending Market (March 2013), the OFT found evidence of widespread non-compliance with the Consumer Credit Act (CCA) and evidence of irresponsible lending. Too many people were given loans they could not afford, and when they couldn't repay were encouraged to extend them, exacerbating their financial difficulties.
- 2.5 As of 1st April 2014, the FCA took over the regulation of around 50,000 consumer credit firms from the OFT. CCA and OFT standards were carried across and became part of the FCA rules and guidance as they were being formed. Part of the FCA's remit in the take-over was to tackle poor conduct in the HCSTC market and ensure consumer protection.

3 Main issues

FCA Changes

- 3.1.1 Following consultation in autumn 2013, from July 2014 the FCA implemented their rules for consumer credit firms, setting out higher standards for payday and other high-cost short-term lenders and for debt management firms. This includes;
- Limiting to twice, the number of times loans can be rolled over.
 - Limiting to twice, how often firms can unsuccessfully attempt to collect repayments from borrowers' bank accounts.

- Clarifying rules on Continuous Payment Authorities (CPA¹) to allow for high-cost short-term loans repaid by instalments.
- Reviewing how borrowers are treated if they are unable to meet their repayments.
- Amending the risk warning that high-cost short-term lenders will have to include on adverts.

3.1.2 Firms with consumer credit licences from the OFT were able to register for 'interim permission' to continue carrying on consumer credit activities from 1 April 2014. All former OFT regulated firms that registered with the FCA before the transfer currently have 'interim permission'.

3.1.3 These firms will be asked to apply for FCA authorisation over the next two years. Every lender with interim permission has been allocated a three month period when they must apply to the FCA for authorisation.

3.1.4 HCSTC firms are among the first to be required to apply for authorisation, and must apply between 1 December 2014 and 28 February 2015. If they fail to apply by the end date then their interim permission will expire and they must stop carrying out consumer credit activities.

3.1.5 As part of deciding whether or not to authorise a firm, the FCA will ask specific questions on firms' business models and strategy, and where they identify risks or problems, they will take action – including refusing permission where necessary – to ensure that firms follow rules and treat their customers fairly.

3.1.6 Once authorised, HCSTC lenders and providers of home-collected credit will have to report product sales data collection of which will begin in October 2014.

3.2 FCA Cap Proposal

3.2.1 In November 2013 the Chancellor of the Exchequer announced that the government will legislate to introduce a cap on high cost short term loans. The cap will be imposed through a legal duty on the FCA, and will be introduced no later than 2nd January 2015.

3.2.2 In July 2014, the FCA published their proposals² for a consultation on the level at which the cap will be set, the deadline for the consultation ended 1 September 2014. They expect to announce the details of the final cap in November 2014.

3.2.3 In introducing a cap on credit, the FCA have defined HCSTC as a loan agreement under 12 months, charging 100% APR or higher. The FCA have excluded home credit, pawn brokers, logbook loans, credit cards, overdrafts and rent to buy lenders from their definition. This means the only lenders directly affected by the cap will be online and retail pay day lenders. The FCA is not looking to widen the

¹ CPA transactions are a form of regular payment, where individuals provide a business with their bank account details and authorise them to deduct a set or variable amount from their account on an ongoing basis. The business can continue to take payments until the agreement with them ends or payment is cancelled. CPAs are different from standing orders and Direct Debits as they do not provide the same level of protection, while allowing the retailer more flexibility in taking payments.

² Proposals for a price cap on high-cost short-term credit, Financial Conduct Authority, July 2014

scope of the definition at this time. Although will be carrying out a wider credit market survey in autumn 2014.

- 3.2.4 In making their proposals the FCA reviewed existing research and liaised with overseas regulators that use a cap; had discussions with industry and consumer groups, collected data from eight HCSTC lenders on 16 million loans to build a model to estimate the impact of their cap; analysed credit records of 4.6 million people who applied for HCSTC loans in 2012 and 2013 and surveyed 2,000 of the applicants in more detail.
- 3.2.5 The aim of this research was to establish what would happen to lending firms as a result of the cap; what options would be available to customers who would lose access to HCSTC as a result of the cap; and would the customers be better or worse off as a result of not having access to HCSTC.
- 3.2.6 With this research, the FCA structured and proposed a cap at three levels:
1. An initial cost cap: set at of 0.8% of the outstanding loan per day, on all interest and fees charged during the agreed loan duration and when refinancing. The initial cost cap will be calculated as a percentage of the outstanding loan according to the number of days of the loan.
 2. A default cap: set at £15, which applies when a customer is in default, The customer can never pay more than £15 in total default fees. When in default, interest is charged at the same rate as the initial cost cap, calculated per day on an outstanding balance and fixed default charges.
 3. A total cost cap: set at 100% of the total amount borrowed applying to all interest, fees and charges. Therefore a customer would never pay more than double the original amount borrowed.
- 3.2.7 The FCA has pitched the cap at £24 for every £100 borrowed over 30 days. If a customer defaults they would never pay more than £15 in total default fees, and if they get into further difficulties, would never pay more than £200.
- 3.2.8 Without taking default fees into account, the FCA estimate that the £24 per £100 borrowed over 30 days is equivalent to 1270% APR. Comparably, the market leader charges 5853% APR, and without a cap in place, other lenders are charging in excess of this.
- 3.2.9 With a cap at this level, the FCA estimates that customers still eligible for HCSTC will benefit from lower prices. Under new capping rules, 11% of individuals (160,000 people a year) who would have been eligible for a HCSTC loan will be declined if they were to apply. The FCA's survey research indicated that it is unlikely these customers would turn to illegal lenders and believe they would benefit from not having access to HCSTC.
- 3.2.10 The FCA expects the cap to reduce the number of online and high street lenders. The FCA's impact model estimates that at the 0.8% initial cost rate, the three largest online firms and one high street firm will be able to continue to offer HCSTC.

3.2.11 The FCA plan to carry out a review of the price cap in two years' time and will continue to review whether they should consider imposing a price cap on other products.

3.2.12 They will also continue to work closely with the Illegal Money Lending team to monitor trends in illegal lending before and after the cap comes into effect, and will take targeted action where necessary.

3.3 Leeds City Council's response to consultation

3.3.1 LCC's response (attached as appendix one) welcomed the evidence based approach the FCA has taken and the fact that HCSTC market consumers were consulted in proposing a cap on payday loans.

3.3.2 Overall, the proposed structure of the cap and the fact that cap covers the total cost of credit is supported, in order to prevent lenders from charging excessive fees. However, there is concern around the level of the cap, which is believed to be geared towards ensuring the HCSTC sector continues to operate rather than prioritising consumer protection.

3.3.3 According to proposals the level of the cap is a balance of a number of factors including "the detrimental impact on consumers of the loss of all HCSTC providers." A key concern of government is also that consumers may face reduced access to credit. However this is at odds with FCA's own findings that:

- Consumers who just qualify for HCSTC would benefit from no longer having access to HCSTC, and;
- Customers with better credit scores would be better off accessing credit from existing lower cost options.

3.3.4 Given these conclusions the FCA should be sending a much clearer message to the HCSTC sector and better protect consumers from harm by setting a lower cap. Furthermore the proposed cap is out of line with caps and rates imposed internationally.

3.3.5 Leeds City Council's Financial Inclusion Team conducted a detailed research study³ into the impact of caps in Europe, Japan, the USA and Australia. This research was published in July 2014, the week immediately following the publication by the FCA of their cost cap consultations. Across the countries analysed for this report, where there is a cap, it does not always include the total cost of credit. In Australia, the cap is set at 48%, but when the total cost of credit is considered, in some cases short term loans in Australia will cost customers up to 300% in interest charges. Similar three digit figures are accepted in the total cost of credit in states across America and countries across Europe. If the UK is to fall into line with most international experience then the cap on HCSTC should be set at somewhere between 24% and 300% APR. A cap set at the proposed 1270% APR (plus default charges) would leave the UK as a complete outlier in the international community.

³ Capping the cost of credit: International evidence, Leeds City Council, July 2014

- 3.3.6 The FCA proposals rely heavily on profit driven lenders being fair to customers. International experiences in countries where caps have been in place have repeatedly shown that lenders are unable to act in this way, and need stringent regulation.
- 3.3.7 Whilst it could be argued that the UK market is different to other financial markets, it is also the case that the financial markets in other countries are also very different from each other. The one thing that is more distinct in the UK compared to other markets is the extent to which the financial market is very lightly regulated. It seems odd to argue that because the UK market is lightly regulated this then prevents more forceful regulation from being considered. Given the considerable evidence that many consumers are suffering serious difficulties at the hands of the HCSTC market then the calls for much tighter regulation should be heeded.
- 3.3.8 The FCA's own research found that many people take out more than one loan with a HCSTC company, and therefore this is not a short term option but used as a means of managing day to day finance. Consideration should therefore be given to supporting more affordable and sustainable credit options. For example, requiring the mainstream banks to be under an obligation to provide financial services in areas with high numbers of low income residents. The aim being to increase not just bank account ownership but more importantly bank account usage and also provide access to low value loans.

4 Corporate Considerations

4.1 Consultation and Engagement

- 4.1.1 The FCA Consultation ended on 1 September 2014. Leeds City Council submitted a response to the FCA attached as appendix one.

4.2 Equality and Diversity / Cohesion and Integration

- 4.3 This report provides details of the actions the FCA has taken to regulate the High Cost Short Term Credit industry since 1st April 2014, and details of their consultation on the proposed cap on the total cost of high cost credit. The FCA's proposal includes a full equality impact assessment.

4.4 Council policies and City Priorities

- 4.4.1 Addressing poverty and deprivation is a key priority for the Council. The LCC response to the consultation on the proposed price cap on high cost short term credit supports the Best Council Plan, the Safer and Stronger Communities Plan, the Children's and Young People's Plan, the Child Poverty Action Plan and the Leeds Joint Health and Wellbeing Strategy. All of these plans have a strong focus on addressing debt, maximising income and moving people and families out of poverty.

4.5 Resources and value for money

- 4.5.1 No implications.

4.6 Legal Implications, Access to Information and Call In

4.6.1 No implications.

4.7 Risk Management

4.7.1 No risks arising from this report.

5 Conclusions

5.1 Since taking over the regulation of consumer credit in April this year the FCA has taken steps to implement higher standards for the HCSTC industry, including the proposals for capping the total cost of credit.

5.2 Leeds City Council submitted response to the consultation on a price cap for the HCSTC market supports the introduction of the cap. However, concern was expressed around the level at which the cap has been set, which appears to be geared towards ensuring the HCSTC sector continues to operate rather than concentrating primarily on consumer protection .

6 Recommendations

6.1 Executive Board is asked to note the content of this report and in particular Leeds City Council's response to the FCA consultation set out in Appendix one.

6.2 The Chief Executive is asked to write to all Leeds MPs asking them to consider Leeds City Council's response to the FCA consultation as set out in appendix one and urge them to take up the issues raised within the Council's response.

7 Background documents⁴

7.1 None

⁴ The background documents listed in this section are available to download from the Council's website, unless they contain confidential or exempt information. The list of background documents does not include published works.

Appendix one

Leeds City Council's response to the FCA consultation paper: Proposals for a cap on HCSTC

Question	Comments
<p>Q1: Do you have any comments on our general approach to developing our proposals for the price cap?</p>	<p>The evidence based approach taken by the FCA to developing proposals for the price cap is welcomed. The detailed quantitative and qualitative data brought together demonstrates a thorough approach. We are pleased that the HCSTC market consumers have been consulted and that the FCA has recognised that many customers of HCSTC are in difficult and deteriorating financial situations. The identification that HCSTC clients are typically younger and have lower savings than average borrowers, use the finance for day to day living expenses and are not coping with their finances, is particularly useful, and supports the findings of our own research conducted into financial exclusion which was undertaken in 2004 and a follow-up study in 2010⁵.</p> <p>However, despite the identification of the harmful impacts of the HCSTC market, the consultation proposals place an emphasis that the regulations should not impede the industry's ability to thrive or cause firms to exit the market. This is at odds with FCA's own findings that for consumers who just qualify for HCSTC would benefit from no longer having access to HCSTC, and that even for customers with better credit scores they would be better off accessing credit from existing lower cost options. Therefore the desire to safeguard these companies from closure, who are profiting from the most financially vulnerable members of our society, is questionable. Furthermore, if as HM Treasury believe the main risk is that consumers faced reduced access to credit, alternative and more affordable sources of credit need to be encouraged, these are not mentioned within the proposals.</p> <p>We would further point the FCA to well researched evidence concluding that the impact of high cost lenders has a negative effect on local economies, draining capital out of communities, particularly poorer communities. A research study undertaken by Salford University on behalf of Leeds City Council in 2009⁶ looked at the Economic Impact of Financial Inclusion Initiatives. The investigation in this study measured the impact achieved resulting from initiatives including the delivery of affordable credit (primarily through credit unions) debt advice and work of Social Landlords in alleviating problems resulting from debt and rent arrears. The research showed that, in those three areas alone, the disposable income of families increased by £9million per year – and that most of this increased disposable income went to poorer communities. The research also found additional benefits such as reduced stress levels, improved health and quality of life, which would have positive economic as well as social impacts.</p>

⁵ Dayson, K & Vik, P (2011) Evolution of Financial Exclusion in Leeds since 2004.

⁶ Dayson et al (2009) Financial Inclusion Initiatives: Economic impact and regeneration in city economies, the case of Leeds

	<p>The international research</p> <p>Although comments are made about international comparisons being ambiguous and requiring caution because market, legal, social structures and regulatory frameworks vary between countries, it was encouraging to see some common lessons identified. It is important that the FCA looks carefully at the international circumvention techniques utilised by high cost lenders in other countries and builds in prevention mechanisms alongside the cap regulations.</p> <p>In July 2014, Leeds City Council’s Financial Inclusion Team released a research report, studying the impact of caps in Europe, Japan, the USA and Australia⁷. Evidence from this report is detailed in the responses to the following questions.</p>
<p>Q2: Do you have any comments on the proposed price cap structure?</p>	<p>Overall we are happy with the proposed structure of the cap and support the fact that cap covers the total cost of credit. We understand the 3 part structure to the cap and think this will help prevent lenders from charging excessive fees. We also agree with the proposal that debt collection charges, including where a third party debt collector levies a direct charge on consumer are included in the cap.</p> <p>Capping the daily interest firms are allowed to charge is a valuable step in ensuring charges don’t become excessive. However, we are concerned about the levels at which the proposed cap has been set, please see response to question 3 below.</p>
<p>Q3: Do you have any comments on the price cap levels?</p>	<p>We are concerned that the current price cap level proposals do not address the Governments policy rationale of ensuring that fewer payday loans customers should get into problems, and instead are geared towards ensuring the HCSTC sector continues to operate.</p> <p>According to the FCA proposals the level of the cap is a balance of a number of factors including “the detrimental impact on consumers of the loss of all HCSTC providers.” A key concern of government is also that consumers may face reduced access to credit. However, as mentioned in response to question one above, this is at odds with FCA’s own findings that:</p> <ul style="list-style-type: none"> • Consumers who just qualify for HCSTC would benefit from no longer having access to HCSTC, and; • Customers with better credit scores would be better off accessing credit from existing lower cost options. <p>Given these conclusions we believe that the FCA should be sending a much clearer message to the HCSTC sector and better protect consumers from harm by setting a lower cap.</p> <p>In the July 2014, Leeds City Council international research study, across the countries analysed, where there is a cap, it does not always include the total cost of credit. In Australia, the cap is set at 48%, but when the total cost of credit is considered,</p>

⁷ Leeds City Council (July 2014) Capping the total cost of credit: International Evidence

in some cases short term loans in Australia will cost customers on average 300% in interest charges. Similar three digit figures are accepted in the total cost of credit in states across America and countries across Europe. If the UK is to fall into line with most international experience then the cap on HCSTC should be set at somewhere between 24% and 300% APR. A cap set at the proposed 1270% APR (plus default charges) would leave the UK as a complete outlier in the international community.

Furthermore, in addition to the proposed cap, the FCA proposals also allow for an additional default charge. If this is factored into the equation (by convention this is not generally included), then in the worst case scenario, the FCA cap would be over 5,000% APR, which is clearly excessive.

The FCAs own evidence (figure 5.2) demonstrates that both first time and repeat consumers of HCSTC are more likely to repay their loans if the interest rate cap were to be set at 0.4% per day. In addition FCA research found that current revenue per loan amounts for HCSTC providers range from 0.4% to above 4% per day. Therefore if consumers are better able to repay loans and companies are able to operate at 0.4% then surely a cap at this level is more appropriate. A 0.4% a day i.e. £12 per every £100 for 30 days provides an APR equivalent of 290% and would bring the UK more into line with the international comparators.

The FCA are concerned that interest rate caps lower than 0.8% would lead to closing down the retail payday lending sector and only leaving a small number of firms operating, and therefore leave a financial market which lacks competition. However, we believe that the emphasis should be placed on consumer protection and not a desire to allow this sector to continue to profit from people in financial difficulties. Furthermore, we should not be looking here simply at competition between a specific group of lenders i.e. primarily payday lenders. The analysis should be looking at the whole of the credit market and controlling the excesses of the payday lending market would enhance competition across the various other sectors of the HCSTC market (including those not currently proposed to be covered by the cap – but see later comments on this).

Evidence from Florida also shows that far from having a detrimental effect on the HCSTL industry, tighter regulation and cost capping can have positive effects. The HCSTC market in Florida continues to flourish but cost capping has resulted in an industry which is more risk averse and therefore ensures that lending is done responsibly. One result has been a lower level of default and bad debt.

The proposed default cap of £15 could be split for lenders to charge £5 in default charges over 3 occurrences, or £5 for a first default and £10 on the second default. If lenders are flexible in this way, the £15 default level is a reasonable cap. The question for the £15 level is whether lenders will be flexible, or try to charge as much as possible, as soon as possible. As the FCA research tested fixed default fee caps ranging from £10 to £40 and found limited impact on firms of these

	<p>various levels. We therefore believe that the FCA should either specify how lenders should charge or set the lower charge of £10.</p> <p>We would also question the rationale set out in the FCA consultation report of imposing a 100% total cost cap because 75% is too complicated to work out. This therefore means that people will be paying more because the FCA believes people would be unable to understand a lower rate, which is at best illogical. On this basis 50% would be equally simple and also cheaper. Therefore a customer borrowing £100 will never have to pay back more than £150. The level of the total cost cap should be based upon known evidence about consumer's ability to repay when set at certain levels. There is little point in setting an arithmetically neat rate if this does not take account of consumer's ability to repay.</p>
<p>Q4: Do you agree with our proposals on repeat borrowing?</p>	<p>No, if a lender is charging prices at the cap, a customer needing a short term loan every month for emergency bills would be paying £24 a month for every £100 borrowed. Even if the affordability tests shows the customer can afford to repeatedly pay these charges, does that mean they should be charged the highest price every time they turn to a particular lender? If a customer borrows from a HCSTC lender and repays that lender in full and on time, they have proved they are not as high risk and do pay their loans off. Therefore, repeat borrowers should be offered lower prices, not the maximum capped price.</p> <p>In addition the FCA should consider a "cooling off period" between discharging one loan and taking out another with either the same or a different lender (perhaps 24 hours). This will reduce the ability of a lender to pressurise a customer to take out additional loans whether this is in the interest of the consumer or not. This facility has been successfully employed in Florida in the USA.</p> <p>The FCA proposals rely heavily on profit driven lenders being fair to customers. International experiences in countries where caps have been in place have repeatedly shown that lenders are unable to act in this way, and need stringent regulation.</p> <p>Whilst it could be argued that the UK market is different to other financial markets, it is also the case that the financial markets in the countries the subject of the Leeds City Council study are also very different from each other. The one thing that is more distinct in the UK compared to other markets is the extent to which the financial market is very lightly regulated. It seems odd to argue that because the UK market is lightly regulated this then prevents more forceful regulation from being considered. Given the considerable evidence that many consumers are suffering serious difficulties at the hands of the HCSTC market then the calls for much tighter regulation should be heeded.</p> <p>FCAs own research found that many people take out more than one loan with a HCSTC company, and therefore this is not a short term option but used as a means of managing day to day finance. Consideration should therefore be given to supporting more affordable and sustainable credit options. For example, requiring the mainstream banks to be under an</p>

	<p>obligation to provide financial services in areas with high numbers of low income residents. The aim being to increase not just bank account ownership but more importantly bank account usage and also provide access to low value loans. The kind of approach adopted in the United States in 1977 by the CRA legislation, would assist in this regard in the UK.</p>
<p>Q5: Do you have any comments on the scope of the price cap?</p>	<p>We are encouraged that FCA have announced the home credit sector, pawn brokers, credit card and overdraft charges, log book loans and the rent to buy market are being reviewed. We believe that these companies should be included within the scope of the cap.</p> <p>We are also supportive of the inclusion of charges made by credit brokers who share some or all of their charges with the lender or those who are in the same group as the lender, however, we would urge that this sector is closely monitored. It is unclear what restriction would be placed on brokers who do not have a direct relationship with the lender. In many, if not most cases, the fees charged by brokers are excessive and are often charged irrespective of whether a loan is actually taken out or not.</p> <p>It is a particular concern that logbook loans may not be regulated in the same way as lenders defined as HCSTC. Logbook lending poses an anomaly in the high cost credit sector. Payday lenders offer unsecured loans, short term at high costs, however logbook loan customers are paying high un-capped interest rates against a loan secured against their car. If such lenders do not fall under the impending regulation, there is a risk of payday lenders widening their product range and entering these markets.</p> <p>The Leeds City Council study also looked at the rates charged and costs associated with home credit. The reason home credit is more expensive is due to the costs associated with providing staff for home visits and collection. Such staffing costs are not prevalent in the online payday market and this raises questions as to why their prices need to be so much more than those charged by home credit companies (bearing in mind that a not for profit model of home credit could operate at something over 123% APR)⁸.</p> <p>Bank unauthorised overdraft charges are not proposed for inclusion in the cap at this stage but this should be subject of urgent attention. Most banks unauthorised overdraft charges are excessive and often massively higher than even the rates charged by payday lenders.</p>
<p>Q6: Do you have any comments on our proposed Handbook rules?</p>	<p>The draft rules have considered avoidance techniques by lenders and stated that in such incidences, where a lender breaches the rules of the cap, the borrower will never pay more than the capped rates. There does not appear to be any real preventative regulation for the lender or any information on tough punishment of lenders who do breach the rules. How will the FCA know when a lender breaches the rules with vulnerable customers? The onus appears to be on the</p>

⁸ Kempson, E., Ellison, A., Whyley, C., Jones, P. (2009) Is a not-for-profit home credit business feasible? York: Joseph Roundtree Foundation

	<p>customer to report such incidents. Will the FCA accept third party references, for example advice agencies?</p> <p>The Leeds research found that tough punishment of illegal lenders; such as longer prison sentences and large scale fines have seen a reduction in illegal lenders in Japan. Illegal lending was linked with a history of organised crime in Japan, and this measure had to be included as part of a package of regulations with the cap. Although the culture of illegal lending is different in the UK, consideration should be given to recommending a tough punishment regime to act as a clear deterrent to any unregulated lenders and work in tandem with the price cap on legal lenders.</p>
<p>Q7: Do you agree with our proposals on unenforceability?</p>	<p>We believe more responsibility should be on the lenders to not breach the cap, or on the FCA to monitor lenders to prevent them from breaching the cap.</p> <p>The proposals suggest that a supervisory model is in place to ensure a lender’s business model has consumer protection as a key feature before the FCA will authorise any credit firm. However the FCA will only monitor a lender’s activity if a consumer reports a breach. The FCA proposals seem to leave responsibility with the borrower to report a breach. The borrower should be able to trust an FCA authorised licenced lender to not over charge them and breach any agreement. Therefore the FCA should be more proactive and carry out secret shopper cases on lenders to ensure they are not in breach of the cap.</p> <p>Account has to be taken of the fact that the majority (by number) of payday lenders are not members of a trade body and therefore any element of self-discipline is absent from most of the participants in the market. Although we support the fact that loan agreements are unenforceable if the price cap is breached, we believe that again there is too much responsibility on the borrower to make sure the lender is not taking advantage of them. The FCA does not seem to go far enough in their regulation to clamp down and punish, fine or suspend lenders who may take advantage.</p>
<p>Q8: Do you agree that we should prevent UK-based debt administrators from enforcing HCSTC agreements on behalf of ECD lenders which include charges in excess of the price cap?</p>	<p>Yes, agree this should be the case.</p> <p>Although most countries across the EU cap their loans between 15 – 200% APR (Iff/ ZEW (2010)), the UK with a high rated cap at 1270% APR is not likely to attract the attention of many EU ECD firms exceeding this high rate. However, all UK lenders should be clearly marked as FCA approved, and when advertising loans, online and through other media, the FCA stamp should be something customers are made aware of.</p>
<p>Q9: Do you have any comments on the proposed approach to data sharing?</p>	<p>Any system which is able to help lenders deliver loans responsibly and ensure borrowers can afford any loans given out is welcomed. We strongly support the implementation of data sharing between lenders.</p>

<p>Q10: Do you agree with the costs and benefits identified?</p>	<p>As indicated in our responses to questions 1 to 9 we broadly agree with the costs and benefits identified for the proposed cap of 0.8% per day. However, the FCA's own research has stated that HCSTC is harmful to customers and therefore we would challenge the desire of the FCA to set a cap which allows the market, as currently established, to exist and thrive.</p> <p>Although the proposed cap will reduce the excessive profits currently made, we believe that they do not go far enough and are indeed out of line with caps and rates imposed internationally. We believe that a cost-benefit analysis on an initial cap at 0.4%, with a 50% total cap and £10 default fee should be undertaken.</p> <p>We also believe that more needs to be done to encourage banks to better serve current HCSTC customers.</p>
<p>Q11: Do you agree with our assessment of the impacts of our proposals on the protected groups? Are there any others we should consider?</p>	<p>Agree with the assessment, no further comments.</p>