Submission to All Party Parliamentary Group on Debt on Personal Finance Inquiry into the Rent to Own Market

October 2014

The Centre for Responsible Credit ('CfRC') is pleased to respond to the APPG on Debt and Personal Finance's call for evidence concerning the operation of the Rent to Own ('RTO') sector in the UK.

We have been active in the study of this section of the consumer credit market for a number of years and have experience of working with both consumer organisations and the three main lenders (Brighthouse, PerfectHome and Buy as you View) in a project undertaken throughout 2011 and 2012 in order to develop a number of customer commitments and 'charters' to improve lending practice. A full report of the outcome of that project[1] can be downloaded from our website.

These commitments were centred on the following 'issues of concern' which customers of the sector had identified. Specifically, these were the need for:

- Greater transparency in the sales process to ensure that customers were advised of the total cost of items, including any optional warranties and insurance products which were offered at point of sale;
- The need for mystery shopping to take place to ensure that sales staff properly explained the cost of agreements to customers;
- The need for staff to encourage customers to consider whether obtaining items on RTO agreements were the best option for them and for RTO lenders to signpost people to independent sources of advice concerning how they might improve their credit rating;
- Ensure that advertised 'cash prices' for goods were comparable with high street stores and were not artificially inflated in order to reduce the apparent APR figure in respect of interest and other charges;
- Firms to provide more, and clearer, information concerning ongoing accounts and in particular to ensure that customers could see how payments had been allocated toward the payment of individual items;

[1] Gibbons, D. (2012). Improving Practice in the Rent to Own Market. Centre for Responsible Credit is available from http://www.responsible-credit.org.uk/projects/developing-a-code-of-practice-for-rent-to-own-lenders

- Firms to make clear the cost of any optional warranties and insurances and to advise people that they may, under some circumstances, find it cheaper to take out a home contents insurance policy rather than the firm's own insurance;

- Firms to refrain from modify existing agreements (e.g. by adding in other items) where the effect would be to extend the length of time that customers have to make payment in order to obtain ownership of the original items;

- Customers to be provided with a clear statement of their rights and responsibilities in relation to the repair and/or replacement of faulty goods and that firms put in place clear customer service standards to ensure that people do not pay for periods of time when they are not able to use the goods;

- Customers to be provided with a range of payment options and benefit from taking out cheaper forms of payment (e.g. direct debit) where these are appropriate;

- Firms to refrain from charging more than the actual cost of default and make sure that they signpost people in financial difficulties to free to use debt advice agencies.

The three firms proceeded to make a number of commitments on these issues (although the specific level of commitment varied between the firms in the project) and embed these into their own 'customer charters', which were to be made readily available on-line and in store (where appropriate[2]). The specific undertakings given by each of the three firms is available in our 2012 report.

, and there is evidence from our ongoing knowledge of Brighthouse's practices alone that the commitments have been broken in a number of important respects:

- The initial customer charter setting out its specific commitments against each of the issues of concern has since been removed from its website and replaced with a bland statement concerning customer service and dealing with people in financial difficulties[3];

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[2] Buy as You View does not operate a store based model.
[3] http://www.brighthousegroup.co.uk/corporate-responsibility/customer-charter/

- Despite assuring us that cash prices for goods would be comparable with high street stores, a recent exercise indicates that a washing machine from Brighthouse carries a cash price of around £300 more than a similar model at Currys;

- Despite noting concerns that people were taking out unnecessary warranties and insurance products, Brighthouse has recently incorporated these into it prices so that they are no longer optional. This has caused its typical APR to rise to 64.7 per cent. A similar approach has now been adopted by PerfectHome which recently abandoned the myth of its ‘optional’ CoverPlus warranty and incorporated this into its now ‘inclusive’ agreement which carries an APR of 59.9 per cent;

Again, it should be noted that there has been no comprehensive audit of the commitments provided by the firms and that further breaches of the voluntary agreement are, in our view, likely to have taken place.

In addition to the failure of this voluntary approach to improve practice, the sector has also not been sufficiently regulated. The Office of Fair Trading was a participant in the project outlined above, but took no action of its own to improve practice or audit firms against the concerns that RTO customer raised. This was despite the fact that during its 2010 review of the High Cost Credit Sector it reported that there was both a lack of transparency in the pricing of RTO agreements and a high degree of dependency on this source of credit amongst RTO customers. And, of course, there have been long standing concerns about the price of credit being paid by low income, often lone parent, households which are the mainstay of the RTO customer base. For example, Mathers & Sharma (2011), in a report for Barnardos, found that people using RTO stores can pay up to £780 more than would be the case if they were able to buy in cash on the high street. Although the prices of RTO agreements (which typically run for 156 weeks) are exceptionally high, they are not covered by the FCA’s proposed total cost cap on High Cost Short Term Cost Credit and other mechanisms to challenge prices (notably through legal challenge under the Unfair Credit Relationship test introduced by the Consumer Credit Act 2006) are not well used by the customer group.

Concern about price – not only for new customers where there may be higher default risks, but also for long standing customers with good repayment records – therefore also loomed large throughout our project, and the firms gave a number of assurances that they would make better use of data sharing through credit reference agencies in order to try to bring these down, especially for customers with a proven record of repayment with them in order to reward this and to build brand loyalty.

To date, however, we have no knowledge that an effective data sharing arrangement[4] has been established by companies operating in this sector, and we have a number of reservations, even greater use of credit referencing information were to be used (as has recently been done by Brighthouse) that it would benefit consumers. These were fully written up in our report published in 2013[5]. With reference to the RTO sector, we reported:

- Consumers are not price sensitive, often preferring speed of decision making and ease of service to cost;
- That existing mechanisms for sharing weekly repayment information through credit reference agencies were not adequate to identify the 'best' payers', and as a result the system does not provide a truly portable record for the purposes of encouraging competition;
- Some RTO lenders may be uninterested in competing on price grounds and could find that the costs of information sharing exceed the benefits – particularly if the information they obtain is not predictive of repayment behaviour (for example, where heavily over-indebted borrowers pay the lender in preference to other commitments because of the collection mechanism or security of the loan on goods)

[4] The main difficulty has been that weekly repayment records are aggregated into monthly 'summaries' for credit reporting purposes. The way that this is done was stipulated by the Competition Commission following its inquiry into home credit. However, the mechanism put in place requires all weekly repayments in the month to have been missed before the monthly summary reports this. So, it is technically possible for seven consecutive weekly repayments to be missed prior to this being notified to lenders through the credit referencing system. Full details are set out in the report footnoted below.

[5] Gibbons, D. (2013). Does Increased Data Sharing Really Benefit Low Income Consumers? Centre for Responsible Credit, available at http://www.responsible-credit.org.uk/projects/does-increased-credit-data-sharing-really-help-low-income-borrowers

- Even if, as Brighthouse reported to us during the course of the project, the use of data sharing does help them to more accurately identify credit risk, there is no certainty that the savings from this will find their way to the customer in the form of lower prices. Although Brighthouse told us that they were thinking about introducing a differential pricing system (to reward regular payers), there is no incentive for firms to pass on the benefits of lower defaults to their customers in those sectors where price competition is particularly weak.

Since the completion of the above projects in 2012 and 2013, we have been involved in supporting the establishment of an affordable, and fairer, alternative to the RTO firms. We have recently been working with Fair For You, which intends to enter this market in 2015. Market research conducted by Fair For You with existing RTO customers indicates widespread dissatisfaction, including in respect of the overall cost of items and:

- The practice of store staff to 'up-sell' items. Customers are persuaded in store that the item they identified on-line as suitable for their needs is not the one they want and are 'guided' towards more expensive models;

- A lack of care for people in financial difficulties, with customers required to pay weekly in store or face high charges per item if they do not make the 4.30pm deadline. We have also uncovered evidence of high pressure tactics, including contacting friends and family, to pursue arrears.

We would be happy to arrange for a presentation of the outcomes from the Fair For You market research to members of the inquiry as part of any oral evidence session if requested.

### What would work?

In our view attempts to improve practice through voluntary agreements with the main RTO firms have failed and there is a need for the new regulator to take action. This should take the form of making RTO specific rules as an addendum to its recent rules for consumer credit firms, which cover issues of responsibility in lending. Those rules need to be based on the 'issues of concern', including price, which customers of RTO firms have been raising for a significant period of time, and it would be a useful starting point for the FCA to undertake research by way of auditing firms against their previous commitments.

In terms of the main pricing issues, the FCA should require RTO firms to ensure that 'cash' prices are genuinely comparable with mainstream retailers, and are not used to artificially lower the stated interest costs. It should also seek to ensure that prices are genuinely reflective of credit risk. In that respect, more work will need to be done to ensure that credit referencing systems are effective in the weekly repayment sector of the market (which includes door to door moneylending), and that 'good payers' are rewarded with reduced prices over time. The FCA should also seek to ensure that the purchase of any additional warranties and insurances is genuinely optional, and remove the bundling of these items at point of sale.

Finally, we consider that increased monitoring and supervision of the sector is required, and the FCA should set out the resources that it will dedicate to this in the coming 12 months.