Financial Conduct Authority
Submission to the All Party Parliamentary Group on Debt and Personal Finance inquiry on rent to own

Background to FCA regulation of consumer credit

On 1 April 2014, responsibility for the regulation of consumer credit transferred from the Office of Fair Trading (OFT) to the FCA. As a consequence, the FCA's regulated population significantly increased by around 50,000 credit firms. Two thirds of our regulated population is now carrying on consumer credit activities.

All firms with an OFT consumer credit licence (including rent-to-own firms) had to register with the FCA for interim permission before 1 April 2014. Interim permission allows a lender to operate legally until either the firm's application for authorisation has been approved, refused or withdrawn; or it does not apply for authorisation when requested to do so. During an application for authorisation we have powers to scrutinise individual firms more closely than the OFT did.

We are managing the process of making all 50,000 firms with interim permission apply for authorisation by instructing firms when to apply over an 18 month period which began in October 2014.

Since 1 April, all consumer credit firms have had to comply with our high-level Principles for Businesses, the FCA's consumer credit sourcebook ('CONC') and detailed requirements in the Consumer Credit Act ('CCA'). These include provisions relating to advertising, APRs, pre-contract information, adequate explanations, assessment of creditworthiness and affordability, credit agreements, right of withdrawal, right of early repayment, statements, arrears and default notices, forbearance and debt recovery. Of particular relevance to rent-to-own firms, where providers use conditional sale agreements, are the protections in sections 90–92 (protected goods) and sections 99–100 (voluntary termination) of the CCA.

It is worth noting that the OFT's prior regulation of consumer credit was constrained by its limited resources and by limitations in its powers. As a result, we have been tackling a number of cases of misconduct by firms. The FCA has a more expansive regulatory toolkit available to it and we remain determined to act decisively where we see evidence of unfair business practices that impact adversely on consumers or the integrity of the market.

FCA views about the rent-to-own market

Our overarching view of this expanding sector is that consumers who use the services of rent-to-own firms are likely to value the ability to buy household items in weekly or monthly instalments over a period of time. As such, rent-to-own is likely to appeal to lower income households who need to spread the cost of any significant purchase and may not have access to mainstream credit via, for example, a credit card or overdraft.

We recently sent an information request to a number of firms operating in the rent-to-own market. All the firms we contacted fully cooperated with our request.

We have a number of concerns over the way that rent-to-own business models operate and the potential risks posed to consumers. Our key conduct concerns are threefold:

- Firm's affordability assessments may be inadequate;
- Firms may be exercising insufficient forbearance to customers struggling to repay; and
- There appears to be a lack of transparency in firms' charging structures and advertising.

In addition, we are concerned that customers using the services of rent-to-own firms may be overly focused on the weekly cost of repayment with little attention paid to the base cost of the item, the cost of add-ons or the total amount payable for the item, including all charges and fees.

Affordability assessments

All consumer credit lenders are required to comply with our rules on creditworthiness, including that the loan must be affordable and sustainable for the individual borrower. The assessment must be based on sufficient information, obtained from the borrower where appropriate and from a credit reference agency where necessary, and taking into account the type and amount of the credit being sought and the potential risks to the customer. We make clear that the risk of credit not being sustainable directly relates to the amount of credit granted and the total charge for credit relative to the customer's financial situation.

The data we have received from the firms raises concerns over the adequacy of affordability assessments being conducted and whether these are in line with our rules. In particular, we are concerned that firms may not be using enough information to make an adequate assessment whether a customer can afford a loan agreement and this is leading to adverse outcomes for customers.

Products bought from a rent-to-own retailer typically have a three-year term. It is concerning that, across the firms we have looked at, the paid-in-full rates for products sold in 2010/11 suggest that around half of customers are failing to repay their agreements in full by the due date.

Forbearance practices

Our rules require that firms must establish and implement clear, effective and appropriate policies and procedures for dealing with customers whose accounts fall into arrears, and the fair and appropriate treatment of customers who the firm understands or reasonably suspects to be particularly vulnerable. Firms must treat customers in default or in arrears difficulties with forbearance and due consideration.

The responses to our information request indicated that firms offer a number of forbearance options including part return of goods, payment freezes and repayment plans. We view these as positive measures to help customers in financial difficulty. However, we are concerned that firms' policies may not be fully embedded in practices, and so outcomes for customers may vary. Including both voluntary and firm-imposed repossessions, the data provided indicates that repossession rates for loans entered into in 2011 could be as high as 22%.

Lack of transparency

Our Principles for Businesses state that a firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading. Other rules expand on this, including in relation to advertising.

We are concerned about levels of transparency in relation to add-on products and services, and whether customers are in effect paying for services they may already have or do not need. This bundling also makes price comparison more difficult. In addition, it may be difficult for customers to compare the cash price of the products (which tend to be significantly higher than those of other retailers) given the way the products are described.

We have also found a number of failings in the financial promotions of rent-to-own firms. These include issues on the transparency of the cost of credit and add-on elements as well as the prominence given to weekly repayments rather than the total cost of the item and the associated credit.

Next steps

Rent-to-own firms, as with other consumer credit firms, will have to apply for authorisation when required to do so. At such point we will assess each firm to ensure it is meeting our rules and threshold conditions for authorisation.

In the meantime, where we have found harm to consumers we have a range of supervisory powers that we can use to address concerns in individual firms. However, for legal and policy reasons we cannot comment on whether or not we have taken action. This is because the Financial Services and Markets Act imposes restrictions on how we can deal with confidential information that we receive. Where, following due process, we impose a public sanction on a firm or individual, it is our standard practice to publicise this in a press notice.

November 2014