

# Tackling loan sharks – and more!

**A consultation document on  
making the extortionate credit  
provisions within the  
Consumer Credit Act 1974  
more effective.**

**No: CCP 007/03**

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# A Consultation Document on making the extortionate credit provisions within the Consumer Credit Act 1974 more effective.

## CONTENTS

<b>1. Introduction and Summary</b>	2
1.1 Purpose of Consultation	2
1.2 What we want from you:	3
1.3 Responses	3
1.4 Consultees	4
<b>2. Scope of Extortionate Credit Provisions</b>	5
2.1 Introduction	5
2.2 Issues	6
2.3 Proposal	10
2.3.1 <i>Statutory Test</i>	10
2.3.2 <i>Regulating terms other than interest rates</i>	12
2.3.3 <i>Controlling Interest rates</i>	13
2.3.4 <i>Responsible Lending</i>	14
<b>3. Potentially detrimental practices</b>	15
3.1 Background	15
3.2 Issues	15
3.2.1 <i>Interest Charges upon default</i>	15
3.2.2 <i>Cost of Credit</i>	17
3.2.3 <i>Transparency</i>	19
<b>4. Procedural Issues</b>	21
4.1 Background	21
4.2 Issues	22
4.2.1 <i>Group claims</i>	22
4.2.2 <i>Dispute resolution</i>	23
4.2.3 <i>Redress</i>	25
4.2.4 <i>Limitation periods</i>	25
4.2.5 <i>Time Orders</i>	26
4.2.6 <i>Time Orders - Scotland</i>	27
4.3 Existing Agreements	28
<b>5. Summary of questions</b>	29
<b>6. Compliance costs.</b>	32
<b>Annexes</b>	33
ANNEX A Consultees Approached	33
ANNEX B The Consultation Criteria	39
ANNEX C Summary of 'Unjust Credit Transactions'	40

# 1. Introduction and Summary

## 1.1 Purpose of Consultation

While it is clear that most lenders lend responsibly, there are some who adopt practices, which may be detrimental to consumers, and it is vulnerable consumers who may be disproportionately affected by such practices. In its election manifesto, the Government made a commitment to tackle loan sharks and a key element in this will be increasing protection for consumers against extortionate credit agreements and reforming the licensing system.

The review of the Consumer Credit Act, which was launched by Melanie Johnson in July 2001 and aimed at delivering this commitment, identified priority areas for reform. They were:

- ❖ Increasing/removing the financial limit and reviewing exempt agreements under the Act;
- ❖ Making the early settlement regulations fairer to consumers;
- ❖ Enabling consumers to conclude credit agreements on line;
- ❖ Changing the licensing regime to target enforcement on keeping the loan sharks out of the market;
- ❖ Making the extortionate credit provisions more effective;
- ❖ Simplifying the advertising regulations and reviewing the rules on APRs; and
- ❖ Simplifying the rules on multiple agreements

In addition to these the Debt Task Force's second report identified a further area for review, which is the form and content of agreements and pre contractual information.

We have already consulted on options for addressing the first four priority areas. This consultation outlines a range of options for improving protection for consumers against extortionate credit agreements and related practices, including consumer redress and alternative mechanisms for dispute resolution. The consultation on the licensing regime, published in January 2003, complements the proposals highlighted in this paper by looking at the regulation of entry into the market and of the conduct of business.

The Consumer Credit Act 1974 ("the Act") already includes provisions intended to provide protection for consumers against extortionate credit but these have not operated effectively in practice and have left vulnerable consumers open to exploitation by lenders. Some of the key issues identified include: -

- ❖ Few cases have reached the courts primarily because the qualifying hurdles for agreements to be challenged are very high, litigation in this area is complex and unpredictable, with the risk for borrowers of a potentially large liability for costs and borrowers are reluctant to pursue such cases through fear of the lender or of the court process.
- ❖ The Act primarily applies to the factors prevailing at the time the loan is taken out but it may be subsequent changes that make an agreement extortionate.

- ❖ A court can only look at the individual agreement and circumstances of that agreement, and its decisions will not directly affect others, which may contain the same terms.
- ❖ A court can only re-open an agreement at the request of the debtor or surety.
- ❖ The focus in dealing with extortionate credit has been primarily on the interest rate when it may often be other terms and conditions of an agreement or business practices which cause detriment.

With the assistance of a number of past studies and working groups held during 2002 with various interested parties we have identified a number of potential options for addressing the deficiencies in the Act. These include:-

- ❖ Replacing the current definition of extortionate credit in the Act with a wider concept to encapsulate unfair practices that are detrimental to the consumer.
- ❖ Enabling consumers to challenge the terms of an agreement or other detrimental practices at any time throughout the term of an agreement.
- ❖ Introducing a dispute resolution mechanism as an alternative to the courts.
- ❖ Empowering the OFT or other qualified entities to seek a declaration in the public interest that a particular credit transaction, or a particular aspect is deemed unfair.
- ❖ Allowing specified third parties to bring actions on behalf of a borrower or group of borrowers e.g. OFT, consumer bodies.
- ❖ Ensuring that lenders provide timely and appropriate information to consumers throughout the entire credit process.
- ❖ Improving the Time Order provisions within the Act so they can be of more benefit to the consumer.

## **1.2 What we want from you:**

The main issues and options are set out in this consultation document, and included are a number of questions on which we want your views. A summary list of the questions is in part five.

We have also published a separate consultation on our review of the licensing regime and this can be found on the link below. Whilst appreciating the burdens that are being put on consultees can we kindly request that responses on these two consultations be documented separately.

To complete the review of the priority issues further consultations will be undertaken through to the summer of 2003. Consultees are therefore asked to confine their responses to just the issue of extortionate credit.

## **1.3 Responses**

You can respond to this consultation by emailing us at Gary.R.Smith@dti.gsi.gov.uk or by writing to Gary Smith, Consumer and Competition Policy Directorate, Room 407, Department of Trade & Industry, 1 Victoria Street, London SW1H 0ET. The deadline for responses is 6th June 2003.

Your response to this consultation document may be made publicly available in whole or in part at the Department's discretion. If you do not wish all or part of your response (including your identity) to be made public, you must state in the response which parts you wish us to keep confidential. Where confidentiality is not requested, responses may be made available to any enquirer, including enquirers outside the UK, or published by any means, including on the Internet.

#### **1.4 Consultees**

We are sending this document to the consultees listed in Annex A. Additional copies of this document may be made without seeking permission. Alternatively copies may be downloaded from the Department's website:

[http://www.dti.gov.uk/ccp/topics1/consumer\\_finance.htm](http://www.dti.gov.uk/ccp/topics1/consumer_finance.htm)

## 2. Scope of Extortionate Credit Provisions

### 2.1 Introduction

Most credit, for most consumers, most of the time causes no problems. However there is an ongoing concern about some activities mainly on the margins of the market that can be described as socially harmful lending, i.e. transactions where the costs of credit (in terms of price and associated terms and conditions) substantially exceed levels which would be generated by a fully competitive market and/or are so oppressive or exploitive that no sensible person, independently advised, would find them acceptable. The proposals in this document are aimed at ensuring that consumers, and particularly the most vulnerable, are adequately protected, while not imposing unnecessary burdens on legitimate lenders.

The issue of extortionate credit has generated a great deal of attention from many interested parties including the media, regulators, consumers and consumer advisors for some years. Back in 1991 an Office of Fair Trading report, 'Unjust credit transactions', reviewed the extortionate credit provisions contained in the Act and concluded that the existing provisions did not provide sufficient protections. A summary of the main recommendations can be found in appendix C. In 1999 DTI commissioned research<sup>1</sup> to follow up the issues raised by the OFT report and in December 2000 NACAB published a report on extortionate credit<sup>2</sup>.

The question of whether credit is extortionate may be seen as limited to the cost of credit but there are other factors, which may be relevant, e.g. the level of default charges, terms relating to how interest is charged upon default and the lack of timely and relevant information for borrowers.

The provisions relating to extortionate credit are in sections 137 – 140 of the Act, which provide that a credit bargain is extortionate if it requires the borrower to make payments, which are 'grossly exorbitant', or it otherwise 'grossly contravenes ordinary principles of fair dealing'. The provisions allow the court, upon the debtor's application, to re-open the credit agreement "so as to do justice between the parties" and set out the relief open to the court. In considering the matter the court is required to take into account certain factors including:

- ❖ Interest rates at the time the agreement is made;
- ❖ The debtor's age, experience, business capacity and health;
- ❖ Financial pressure i.e. how desperate the consumer was for credit;
- ❖ Degree of risk accepted by the lender, having regard to security; and
- ❖ Any other relevant considerations.

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<sup>1</sup> From 'Extortionate credit in the UK' – Elaine Kempson and Claire Whyley (Personal Finance Research Centre - June 1999)

<sup>2</sup> Daylight Robbery – The CAB case for effective regulation of extortionate credit – Published December 2000

Our understanding is that since 1977, when the provisions came into force, the courts have decided less than 30 cases and most of these have involved non-status secured lending.

It is borrowers in the non-status sector of the market who are likely to be most at risk, due to the consumer's impaired or low credit rating, which makes it difficult to obtain finance from traditional sources on standard terms and conditions. The concern was such that in 1997 the Office of Fair Trading published guidelines for lenders and brokers concerning non-status secured lending<sup>3</sup>.

The European Commission has recently published a proposal for an amended Consumer Credit Directive. There are no specific articles relating to extortionate credit although there are articles relating to lenders being able to demonstrate that they have lent responsibly and a number of contract terms are defined as unfair e.g. varying any contractual costs or charges other than the borrowing rate and introducing rules on the variability of the borrowing rate that discriminate against the consumer.

We will need to ensure that our proposals can be implemented in compliance with Community law.

## **2.2 Issues**

The 1999 DTI research followed the OFT's re-presentation to Ministers of its 1991 report entitled "Unjust Credit Transactions", and subsequent work on non-status lending which highlighted substantial evidence of the continued existence of serious problems for consumers in the UK, which consumers are most at risk and what steps could be taken to alleviate the problem. The research found that only a relatively small number of people had loans whose costs, terms and conditions would be considered extortionate however defined but these were the most vulnerable people in society. In addition, several million more people had loans with specific terms and conditions that could be considered extortionate, even though they were dealing with reputable companies. Those most affected fell into two groups – people living on very low incomes who required small loans for short periods of time, and people with a history of bad debt and County Court Judgments (CCJs) who were often seeking secured loans to consolidate their debts.

Practices highlighted by the research as problematic included lack of transparency, providing high cost loans to consumers who had little choice of credit providers, rollover loans, failure to check a borrower's ability to repay and consolidating a number of loans into a single secured loan. The report also concluded that few cases are brought to court (less than 30 since 1977) because the onus rests with the borrower to initiate proceedings or issue an application in proceedings brought by the lender. The research suggests the consumers most affected by unscrupulous lenders will not have the resources or will feel vulnerable and afraid of taking court action.

The NACAB report 'Daylight Robbery' concluded that: -

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<sup>3</sup> Non-status lending Guidelines for lenders and brokers – published by OFT in November 1997

- ❖ Problems of extortionate credit persisted.
- ❖ Extortionate credit arose from either unduly high interest rates or from loans that put the borrower at a significant and unfair disadvantage against the lender. The report provided details of cases from all over England and Wales where extortionate credit agreements were enabling some creditors to take advantage of uninformed consumers.
- ❖ CAB evidence showed that extortionate credit agreements existed across a range of credit products and agreements. The greatest concerns appeared to relate to secured lending (particularly debt consolidation loans), lending to low income groups, lending attached to the sale of cars and home improvements, and lending to those with impaired credit records.
- ❖ Existing legislation on extortionate credit was neither effective nor accessible to consumers. The current 'test' that determines whether a credit agreement is extortionate was heavily weighted in favour of lenders. Moreover, the test could only be invoked if a borrower was prepared to risk heavy legal costs in taking the initiative and making an application to the court.

During 2002 we undertook discussions with representatives from amongst others, the lending industry, consumer bodies, regulators, legal experts and district judges on the current problems being experienced. As a result of this and of consideration of correspondence and publications on this issue we have identified a number of key issues. These are: -

- ❖ The qualifying hurdles for agreements to be challenged are generally considered to be too high. It has also been argued that the wording of the Act is imprecise leaving it difficult for consumers or their advisers to assess the likelihood of being able to successfully challenge an agreement.
- ❖ Litigation in this area is complex and unpredictable with the risk for borrowers of a potentially large liability for costs.
- ❖ Borrowers are reluctant to pursue such cases through fear of the lender or of the court process.
- ❖ Borrowers may be unaware that they may have a claim due to the lack of publicity, or cases being settled out of court and subject to a 'gagging' clause.
- ❖ The provisions of the Act largely only apply to the factors prevailing at the time the loan is taken out. This means that a lender may be able to vary terms post agreement without risk of them being challenged as extortionate. A problem can also occur when the terms are not changed in line with market conditions. A recent court case<sup>4</sup> highlighted this problem where the lender failed to reduce interest rates at a time that rates were falling in the market therefore widening the differential that was charged.

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<sup>4</sup> Paragon Finance PLC v Nash and Staunton – 15<sup>th</sup> October 2001

- ❖ The court can only look at the individual agreement and circumstances of that agreement, and its decisions will not directly affect others, which may contain the same terms.
- ❖ A court can only re-open an agreement at the request of the debtor or surety, many of whom are not aware of this right or who at a time of distress may not turn up at court.
- ❖ The focus in dealing with extortionate credit has been primarily on the interest rate when it may often be other terms and conditions of an agreement, or business practices, which cause detriment. For example levels of security required, conversion of unsecured to secured loans following default, terms relating to how interest is charged upon default which may result in rapidly increasing the debt owed, and the lack of timely and relevant information being sent to a borrower, and
- ❖ Little use is made of the provisions in the Act for time orders. These could in some circumstances give consumers the opportunity to seek an extension to the repayment period, reduce the required monthly payment for a period of time and prevent debts increasing after the court has determined an appropriate level of payment.

### **Current Provisions**

The Act currently states that a credit agreement is extortionate if:

- ❖ It requires the borrower to make payments which are grossly exorbitant; or
- ❖ Otherwise grossly contravenes ordinary principles of fair dealing.

The provisions in the Moneylenders Acts 1900 and 1927 which preceded the Consumer Credit Act, provided that a rate charged over 48% was prima facie excessive and the transaction '*harsh and unconscionable*' enabling a court to reopen the agreement. Although the report of the Crowther Committee<sup>5</sup> on which the Act was based, recommended retaining this wording it was changed for the Act and the new wording has proved to be a high qualifying hurdle.

The factors to which the court must have regard in determining whether a credit bargain is extortionate are listed in sections 138(2) to 138(5) and include: -

- Interest rates prevailing at the time the agreement was made;
- The age, experience, business capacity and state of health of the debtor;
- The degree to which, at the time of making the credit bargain, the debtor was under financial pressure, and the nature of that pressure;
- The degree of risk accepted by the creditor, having regard to the value of any security provided;
- The relationship between creditor and debtor;

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<sup>5</sup> The Crowther Report was published in March 1971 which was commissioned to reform the laws of consumer credit and formed the basis of the Consumer Credit Act 1974

- Whether or not a colourable cash price was quoted for any goods or services included in the credit bargain.

The application of the current provisions has concentrated on the cost of credit despite the fact that the Act provides for other factors to be considered. Whatever test is set, however, has to be sufficiently flexible to accommodate different market sectors.

There has been widespread criticism of the fact that the extortionate credit provisions of the Act primarily apply only to the factors prevailing at the time the loan is taken out. A recent court case where the lender failed to reduce its rates to customers in line with falls in the market rates, many of whom were 'captive' and unable to re-mortgage elsewhere, has highlighted this issue.<sup>6</sup>

Post agreement a lender may be free to vary or apply the terms/interest rate to the detriment of the borrower in a way, which may be extortionate. Examples could include variation in the form of charges and costs, or failing to move with the market when there are large changes in interest rates. Case studies provided show that there may be particular problems in respect of non-status secured loans where the borrower may have no access to alternative forms of credit and finds these factors result in the debt increasing, possibly ending in repossession.

The Unfair Terms in Consumer Contracts Regulations 1999 ("UTCCRs") provide some additional protection. These Regulations apply to unfair terms in consumer contracts. They provide that an unfair term is one which has not been individually negotiated and which, contrary to the requirement of good faith, causes a significant imbalance in the parties' rights and obligations under the contract to the detriment of the consumer. Schedule 2 to the Regulations contains an indicative list of terms, which may be regarded as unfair. The assessment of fairness will take into account all the circumstances attending the conclusion of the contract. However, it does not relate to the core terms of the contract or the adequacy of the price or remuneration, as long as the terms are in plain, intelligible language. Unfair contract terms are not binding on the consumer. The OFT may seek an injunction to prevent the continued use of a term or of a term having a like effect.

Although the UTCCRs provide some additional protection since the extortionate credit provisions came into force, they do have limitations, and we consider that reliance on them, along with the current provisions in sections 137-9 would not provide sufficient protection. In particular, they apply only to agreements which are not individually negotiated, and which are made with consumers (so sole traders and unincorporated bodies would not be protected). The protection for core terms (such as the interest rate) is limited. The Regulations apply only to terms, not practices. The remedial powers under the UTCCRs are more limited than under the current, and proposed, extortionate credit provisions. Although the UTCCRs provide a valuable protection for consumers, we consider that the particular issues and problems raised by extortionate credit warrant additional tailor-made provisions. We therefore do not propose to rely on the UTCCRs, or to adapt them, to provide protection against extortionate credit.

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<sup>6</sup> Paragon Finance PLC v Nash and Staunton – 15<sup>th</sup> October 2001

What we want to achieve is a competitive credit market that continues to provide benefits to both lenders and consumers but with regulation that can be properly targeted on extortionate practices as well as providing appropriate redress for consumers who have suffered detriment.

## **2.3 Proposal**

### **2.3.1 Statutory Test**

The term 'extortionate', by definition, is likely to be seen as concerning the cost of credit whereas the legislation needs to provide wider protection to ensure that the agreement and how it is applied is fair to both parties.

The Act currently states that a credit agreement is extortionate if: -

- ❖ It requires the borrower to make payments which are grossly exorbitant; or
- ❖ Otherwise grossly contravenes ordinary principles of fair dealing.

We propose to build on the recommendations from previous work undertaken in this area and reform the existing provisions by:-

- A) *Replacing the existing definition of section 138 with a wider test such as whether or not an agreement is an 'unfair credit transaction'. The legislation would set out the factors to be taken into account by the courts in determining whether or not a transaction was unfair (see below) but would not otherwise define the term. This test would be less stringent than the current provisions.***
- B) *Extending the factors in sections 138(2) – (5) (see paragraph 2.2.7 above) that the court can consider to: -***
  - Whether the debtor was required to make payments that were excessive;
  - Whether the interest rate charged both at the date of the bargain and subsequently is excessive having regard to interest rates applying to:
    - Borrowers in the market generally,
    - Borrowers in that particular sector of the market, and
    - Other borrowers of the particular credit provider.
  - The extent to which any costs and charges are reasonable having regard to:
    - The interest rate being charged under the agreement;
    - Whether such costs and charges represent the actual loss incurred by the creditor arising out of the debtors default;
    - The extent to which the debtor was made aware of such costs and charges both at the date of the agreement and during the period of the loan.

- Whether the transaction involved any business behaviour or activity of the lender (or broker) which was deceitful or oppressive, or otherwise unfair or improper (whether lawful or not);
- The borrower's age, experience, business capacity and state of health;
- The nature and degree of financial pressure to which the borrower was subjected at the time the agreement was made;
- The lender's care and responsibility in making the loan, including the enquiries which, having regard to all the circumstances of the transaction, the creditor made to ensure that the debtor could afford the loan repayments;
- The degree of risk accepted by the lender, having regard to the nature and value of any security;
- The lender's relationship with the borrower;
- Whether or not a colourable cash price was quoted for any goods or services included in the credit transaction; and
- Any other relevant consideration, such as whether linked transactions had been reasonably required.

**C) *Provide for the court to be able to consider all the factors in B above, as they stand at any time during the agreement.***

As an alternative to listing the factors in the Act, they could be set out in secondary legislation; this would enable changes to be made relatively quickly should the need arise. Although one of the factors includes "any other relevant consideration" and therefore such an approach may not be necessary, it would enable specific issues to be detailed.

We believe that this overall approach will lower the test sufficiently to enable debtors to more easily challenge the terms of an agreement on a wider foundation than just cost. Whilst the vast majority of the credit industry lends responsibly we believe that the revised provisions will deter more strongly the socially harmful lending that occurs at the margins of the credit market without imposing additional burdens on responsible lenders.

**Question 1: Do you agree that by amending the provisions of the Act as proposed above it will enable agreements to be more easily challenged as being extortionate in a way which balances the interests of borrowers and lenders appropriately?**

**Question 2: What factors do you consider should be taken into account in assessing whether or not a credit transaction is unfair? Is there a need for any further definition of "unfair credit transaction" either in the legislation or otherwise fleshed out in guidelines?**

**Question 3: Are there any reasons why the factors in section 138(2) – (5) should not be relevant during the full term of the loan, and if so why?**

**Question 4: Do you support the principle of removing the factors from primary legislation into secondary legislation? What are the pros and cons of each alternative?**

### ***2.3.2 Regulating terms other than interest rates***

It is very common for agreements to be referred to as being extortionate purely on the interest rate that applies but case studies provided indicate that often it is other terms and conditions of the agreement that make it problematic.

In November 1997 the OFT published non-status lending guidelines for lenders and brokers to try and address the problem of certain practices it considered unfair or unreasonable. The guidelines highlight some of the main practices in the secured non-status lending market that may be considered to be deceitful or oppressive, or otherwise unfair or improper, within the meaning of section 25(2) of the CCA, and which could lead the OFT to take licensing action against those involved<sup>7</sup>.

As part of this review we aim to ensure that there are appropriate means to deal with unfair or unreasonable practices with and we see the following as a package to achieve this objective:-

- ❖ The proposals in 2.3.1 taken together with the UTCCRs should deal with any terms and conditions of agreements or practices which are unfair and improper.
- ❖ Unfair practices will also be tackled by the licensing regime, which will be strengthened by the proposals in our consultation on licensing. These include : -Fines – appropriate for breaches of the licence that do not call into question the licensee’s continuing fitness to conduct consumer credit business. If set at an appropriate level, such fines would deter breaches of licensing rules.
  - A process for attaching conditions to the licence – setting out how the licensee will be expected to conduct his business; prescribing certain areas of consumer credit business that the licensee is not permitted to engage in.
  - Enabling or requiring the DGFT to lay down statutory rules of conduct, breach of which may lead to licensing action, including fines. The FSA is able to issue conduct of business rules and associated guidance subject to prior consultation and cost – benefit analysis.
- ❖ Introduce an independent redress mechanism that can assess conduct against fairness principles. (See later proposals on introducing a dispute resolution body).

Whilst considering these options it also needs to be taken into account that the European Commission has made a commitment to propose a framework Directive containing a “general duty not to trade unfairly”. This Directive is likely to cover the selling practices associated with business-to-consumer

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<sup>7</sup> Non-status lending guidelines for lenders and brokers page 1 – published by OFT November 1997

transactions, and will possibly cover consumer credit. The Directive might also require a high level of harmonisation amongst member states, which could mean that any national provisions put in place will need to be amended at a future date. There is an argument therefore to wait and see what the General Duty proposes, but given the uncertainty regarding timing and scope, this will delay introducing increased protections for consumers and therefore is not considered an option.

**Question 5: Given the above do you feel any additional provisions are required in the CCA to deal with unfair practices?**

### **2.3.3 Controlling Interest rates**

It has been suggested that one mechanism for controlling the cost of credit is to limit the rate of interest charged. However it is important to first distinguish between an interest rate and an APR (annual percentage rate) the latter of which includes charges related to the borrowing. Many of the case studies were based on the APR but a high APR does not necessarily indicate that the lending is extortionate. For example, many short-term, small value loans have very high APRs, but these can reflect the short-term nature of the loan and the costs and risks associated with that type of lending.

We have traditionally been against the application of interest rate ceilings for the UK market on the grounds that: -

- ❖ Interest rate ceilings can result in rates gravitating towards that ceiling, and it becoming the market rate.
- ❖ Creditors may determine that they are unable to lend within that ceiling to particular groups of consumers, and withdraw from the market place, often to the disadvantage of the most vulnerable consumers who don't have a ready access to alternative forms of credit, and may as a result be driven to using illegal lenders.
- ❖ Member states with rate ceilings often have a lighter regulatory regime than the UK for non-mainstream lending.

Citizen's Advice has also been opposed to the introduction of interest rate ceilings. Its report<sup>8</sup> concluded that the introduction of an overall interest rate ceiling could potentially prevent certain types of agreements, with lower rates but other detrimental factors, being challenged. They were also concerned that the growth in unregulated and unlicensed lending could be fuelled by imposing a ceiling. It is feared that introducing ceilings could result in some lenders pulling out of some market sectors and as a result could lead to the exclusion of those vulnerable consumers from mainstream lending.

An alternative to an interest rate ceiling is the introduction of presumptive rates. These could set 'acceptable' rates for different types of lending, which could only be exceeded by lenders where prior approval had been granted by a body such as the OFT, or where they could be open to challenge on extortionate credit grounds. They might be imposed through conditions on the consumer credit licences of individual lenders to allow the flexibility to address

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<sup>8</sup> From 'Daylight Robbery' – The CAB case for effective regulation of extortionate credit (Published December 2000)

different markets and types of lending. The disadvantage of this approach is that it would be cumbersome, would require extensive monitoring of rates, and only addresses the cost element of the loan.

Taking all factors into account and the proposed changes to the Act we are not convinced that there is a need to specifically control interest rates in legislation. Our preferred approach is not to over regulate the market, but instead to make it easier for any term within an agreement, including that of price, to be challenged. We would, however, welcome your views on this.

We will be carrying out further research into the way that interest rate controls have worked in other countries across the entire spectrum of their consumer credit markets. This research will also look at the differences in the environment between the UK and those countries, for example in the level of availability of non-commercial sources of credit such as credit unions.

**Question 6: Do you consider that controlling the cost of credit with specific provisions relating to interest rates should be used in the UK credit market; if so please explain the most appropriate mechanism and provide substantiated arguments to support your view?**

#### ***2.3.4 Responsible Lending***

Consideration has been given to incorporating within the legislation provisions to ensure lenders lend responsibly. The recently published draft Consumer Credit Directive has proposed introducing a 'responsible lending provision requiring the lender to demonstrate it had assessed the ability of the borrower or guarantor to discharge their obligations under the agreement. Also the FSA has proposed including responsible lending provisions within their mortgage regulation. Namely that:<sup>9</sup>

- ❖ A lender must be able to show that, before deciding to enter into a mortgage or make a further advance, account was taken of the consumer's ability to repay the loan;
- ❖ Adequate records must be kept to demonstrate that they had taken account of the consumer's ability to repay the loan; and
- ❖ In the absence of evidence to the contrary, a lender should assume that any regular mortgage payments would be met from the consumer's income.

An alternative is to include, as an additional 'factor' (see part 2.3.1), whether the lender had acted irresponsibly.

We would welcome your views on the alternative approaches to ensuring that lenders must act responsibly.

**Question 7: Which of the approaches outlined above requiring lenders to lend responsibly do you think would best meet the needs of consumers and business? Are there other alternative approaches which would be preferable and, if so, why?**

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<sup>9</sup> From CP146 published by the FSA August 2002

## 3. Potentially detrimental practices

### 3.1 Background

As has been mentioned previously, whether or not an agreement is extortionate is often judged purely on the interest rate that applies but case studies provided indicate that often it is the way that other terms, conditions and practices are operated that can make an agreement problematic. These include: -

- ❖ Interest Charges upon default;
- ❖ Charges that can apply during the agreement;
- ❖ The lack of transparency in business dealings.

The situation is exacerbated by the fact that the court can only look at the agreement as it stood at the time the loan is taken out. This means that a lender can vary the terms post agreement without risk of them being challenged as extortionate and it is difficult to challenge the way the terms are applied.

The principle of when an agreement can be challenged is covered in the last section. Here we look at what other issues are experienced by consumers, which may be regarded as 'extortionate', and are particularly prevalent when a consumer falls into arrears.

### 3.2 Issues

#### 3.2.1 *Interest Charges upon default*

One of the areas of greatest concern is the impact on consumers of the way that some lenders charge interest on sums unpaid in breach of the agreement ("arrears"). A number of case studies show how debts have increased significantly during times of default, even when court orders are complied with.

Each month interest will be charged on any outstanding arrears and accrued interest on these sums, and gets added on each time. This is known as compound interest. If the borrower does not increase the contractual monthly payment to accommodate this interest then the debt is ever increasing. As a result a debtor can owe significantly more than expected. Arguments against this practice include: -

- ❖ The interest rate prevailing under the agreement will to some extent reflect the risk to the lender but this may be across an entire loan book rather than by reference to an individual borrower. To permit interest to be charged on arrears and then interest on that interest could be interpreted as double recovery.
- ❖ The lender may impose default charges and monthly arrears tariffs to recover costs. Some consider that the contractual rate of interest, especially when the rate is a high one, already reflects the risk of default.

- ❖ Any additional compensation to the lender by way of interest on arrears should be directly linked to the lender's actual loss. Charging additional interest at the contractual rate for the period that each instalment remains unpaid may not bear any relationship to such loss. This is especially so where the rate is high.

A number of cases provided showed total interest payable as much as four times that which would have been paid had the loan run its normal course without default. The following is just one of many examples highlighted.

A loan for £9,750 (including £750 brokers fee) was taken out in November 1991. Payments were £276.25 per month over 10 years at an annual percentage rate of 42.22%. If the borrower had made all payments on time the total amount payable would have been £33,150. However, there was a history of arrears and court action ensued. Legal fees and collection charges were debited to the account as well as interest on the arrears and the default costs. As at December 2002 additional default interest had built up to £97,189.85 and on top of this there were disbursements relating to legal/collection costs of £9,943.90. Although the borrower had repaid £32,691.25, nearly the full amount they were originally required to repay - the settlement figure was £107,592.50. Payment for this amount would mean that the borrowers would have paid £140,000 over eleven years for a loan of £9,750. The other issue is that as at December 2002 monthly interest in excess of £1,600 was being added to the debt whereas to the contractual payment required was only £276.25.

This example also shows the impact on a debt of the interest being charged on arrears on a compound basis resulting in the interest each month being nearly six times greater than the contractual monthly payment. As a result, the debt continually increases despite the contractual payment being made. In these circumstances the lender will not be charging interest in breach of section 93.

This section of the Act prohibits a lender from charging interest on arrears higher than the rate prevailing in the agreement. In effect this provides a ceiling on the rate of interest that can be charged on default. There are a number of issues that need reviewing and these are: -

- ❖ Whether lenders should be entitled to increase the rate in the event of default.
- ❖ Whether lenders should be required to charge a lower rate on arrears.
- ❖ Whether lenders should be able to charge interest upon interest i.e. on a compound basis.
- ❖ Whether in addition to charging interest at the contractual rate on the balance outstanding including any arrears, should the lender also be entitled to impose a separate arrears charge?
- ❖ Should the lender be permitted to charge any interest on outstanding fees or charges?

Clearly lenders must be permitted to recover costs on arrears, however, it is arguable that these should be limited to recovering reasonable costs and not to the contractual rate of interest (as permitted in Section 93), particularly

when the rate is a high one, as this could result in over-recovery. In these circumstances any 'loss' to the lender would be difficult to predict and we therefore welcome views on how best to limit the amount of recovery further than the current provisions permit.

With regards to any costs that are not included in the original total charge for credit, e.g. separate charges associated with debt recovery, it is arguable that a borrower should have a short period of time e.g. 28 days, following a charge being debited to an account in which to pay before interest is charged, and that the rate is again restricted as in the previous paragraph.

Our reasoning behind this approach is that the contractual rate being applied to the loan already takes into consideration the risk of the lending.

We therefore propose to amend the legislation so as to: -

- ❖ Restrict the rate of interest chargeable on arrears further than currently permitted in Section 93 of the Act. (This currently restricts the rate to the contractual rate).
- ❖ Allow interest to only be charged if the charge/fee (i.e. a sum not included in the total charge for credit) remains unpaid after a specific time period.
- ❖ Prohibit the charging of interest on a compound basis.

**Question 8: Do you agree that prohibiting the charging of interest on a compound basis would be a fair and effective control against the escalation of debts? If not, what alternative would you propose?**

**Question 9: Can you please provide an estimate the cost implications of prohibiting interest being charged on a compound basis?**

**Question 10: Do you consider there should be any restrictions on the interest charged on arrears? If so in what way should it be limited?**

**Question 11: Similarly do you consider there should be any restriction on interest charged on charges and fees? If so in what way should it be limited?**

**Question 12: Should all charges/fees be subject to a restriction on the interest that can be charged or is there a case for some to be excluded? If so, what charges/fees should be excluded?**

**Question 13: What do you consider a fair and reasonable period to allow before interest can be charged on any charges imposed beyond the initial charge for credit?**

### **3.2.2 Cost of Credit**

Although the cost of credit is primarily linked to the rate of interest charged money advisors have raised concerns regarding other costs and charges particularly those relating to default. Some lenders will have a published tariff of charges detailing specific fees whereas others will rely on the general provisions in the credit agreement to recover cost and charges incurred.

Charges tend to come within the following categories: -

- ❖ Charges relating to arrears work undertaken e.g. letters sent, telephone calls made, home visits.
- ❖ Monthly charges or fines where an account is in arrears.
- ❖ Legal costs and other disbursements incurred by the lender in taking recovery action.
- ❖ Costs of responding to requests for more general information on an account e.g. statements.

In principle under the current legislation, borrowers have protection under the extortionate credit provisions, since excessive charges might be regarded as 'grossly exorbitant' under section 138(1)(a) or their imposition as 'grossly contravening ordinary principles of fair dealing' under section 138(1)(b). Our preliminary view is that the proposals put forward in section 2.3.1 above will adequately address any problems of unreasonably high charges in these areas.

There are alternatives to the proposed approach. The Financial Services Authority has sought to address this issue in their proposed regulation of mortgages by requiring that any sums payable on default must not exceed a genuine pre-estimate of the lender's loss arising from breach of the borrower's contractual duty. This allows for cost differentiations across the industry both now and in the future.

An alternative method would be to set tariffs in either legislation or guidelines. We do not consider this would be an efficient mechanism since it would not be able to take account of the different cost bases of different lenders and, if set to accommodate those with the highest costs, would give potential for over-recovery by many lenders. If the charges were too low some lenders may need to increase the interest rate to cover their costs. In extreme cases this may have an impact on their competitiveness in the market leading to them withdrawing. The added issue is that the publication of charges in any form would be very complex, will be a cumbersome and expensive exercise and it will require extensive monitoring of costs across the market and frequent updating.

An alternative is to consider whether lenders should be precluded from imposing arrears charges, or particular types of charge, but instead having the additional costs absorbed into the interest rate. This may provide a more accurate cost of borrowing as there are no hidden costs, but does result in most borrowers subsidising the few that default. There is also an argument that by spreading the cost in this way it reduces the incentive for borrowers to maintain payments.

**Question 14:** Do you consider redefining the extortionate credit terms of the Act as proposed in section 2.3.1 above is sufficient to ensure that charges on arrears cannot be levied at an unreasonably high level?

**Question 15:** If not, what alternative controls do you consider should be applied?

**Question 16: Should lenders be permitted to make charges in certain circumstances or should all costs be absorbed into the interest rate?**

### **3.2.3 Transparency**

A major concern of consumer groups related to situations where borrowers were not given sufficient information about their loans. Examples highlighted include:-

- ❖ Failing to explain at the start of the loan the lender's entitlement to impose charges (particularly when in default) and the circumstances in which they may arise.
- ❖ Failure to provide clear information to the borrower on any charges that may be levied and when they may apply.
- ❖ Charges being imposed on the borrower without notification and without being informed of the implications of interest accrual.
- ❖ Borrowers not being advised of the effect of underpayment and any need to subsequently amend the monthly instalment depending on when the loan is expected to be repaid.
- ❖ Regular statements not being provided unless specifically requested or statements not being clear and complete which would alert borrowers to the existence of any costs, impact and balance of the account.

In October 2000 the Task Force on Overindebtedness was set up to address concerns about consumer debt in the UK by considering ways of achieving more responsible lending and borrowing. In January this year Melanie Johnson published a response to the second report of the task force and this included a recommendation that as part of this review there will be a further consultation on pre-contract information, and the format and content of credit agreements, which would aim to address some of these problems. Details of the full report can be found on:

[http://www.dti.gov.uk/ccp/topics1/consumer\\_finance.htm](http://www.dti.gov.uk/ccp/topics1/consumer_finance.htm)

However, this would not address the cases where borrowers have been unaware of the way in which their debts are accumulating as a result of the addition of default interest and costs, even where the case may have been subject to a court order, which provides for regular monthly payments but this may be less than the rate at which interest is accruing.

Although there are some provisions within the Act that impose certain duties on lenders to provide information to a borrower for a nominal fee, there is no obligation for a lender to provide regular statements for an account to debtors (other than in the case of running account credit) unless specifically asked. As a minimum it has been suggested that in addition to the current provisions for running account credit, that the borrower should be entitled to an annual statement at no cost (and possibly more regularly whilst an account is in arrears), which should include the following details: -

- ❖ An opening balance (which should be the same as the closing balance from the previous years statement).

- ❖ A list of all credits (payments) to the account.
- ❖ A list of all debits to the account (including all interest debited and costs and charges).
- ❖ The current interest rate and any variations during the year.
- ❖ A settlement figure as at the year-end.
- ❖ If any fees and charges have been incurred an explanation about what they relate to.
- ❖ If the balance due will not be repaid by the expiry date of the loan at the current level of repayments, an indication as to the amount the debtor needs to increase the monthly payment by in order to repay the loan by the expiry date.
- ❖ The closing balance.

It is acknowledged that providing all the above information more often than annually may however be excessive.

We are also considering requiring lenders when they debit the loan account with costs or charges to provide the debtor immediately with a notice containing the following: -

- ❖ A statement of the amount that has been debited, what it relates to and the provision in the loan agreement, which entitles the creditor to impose the charge.
- ❖ If interest is to accrue on that cost or charge, a statement to that effect.
- ❖ If interest is to accrue, a statement showing how much interest would be payable on the amount debited and the rate at which it is charged.
- ❖ An explanation that the debtor has the right to repay the cost or charge debited to the loan account at any time.
- ❖ Notice of any interest free period as proposed in section 3.2.1.

We are aware that in some circumstances some lenders charge a monthly 'arrears' fee and it would need to be considered as to whether a notification was applicable each month or at some other reasonable frequency.

**Question 17: Do you consider that there is a need to specify in legislation the frequency and content of account information?**

**Question 18: What and how regularly should information be provided?**

## 4. Procedural Issues

### 4.1 Background

The Act already includes provisions intended to provide protection for consumers against extortionate credit but these have not operated effectively in practice and have left vulnerable consumers open to exploitation by lenders. As we have previously highlighted some of the key issues identified include: -

- ❖ Few cases have reached the courts primarily because the qualifying hurdles for agreements to be challenged are very high, litigation in this area is complex and unpredictable, with the risk for borrowers of a potentially large liability for costs and borrowers are reluctant to pursue such cases through fear of the lender or of the court process.
- ❖ The Act primarily applies to the factors prevailing at the time the loan is taken out but it may be subsequent changes that make an agreement extortionate.
- ❖ A court can only look at the individual agreement and circumstances of that agreement, and its decisions will not directly affect others, which may contain the same terms.
- ❖ A court can only re-open an agreement at the request of the debtor or surety.
- ❖ Little use is made of the provisions for time orders, which could in some circumstances give consumers the opportunity to seek an extension to the repayment period, reduce the required monthly payment for a period of time and prevent debts increasing after the court has determined an appropriate level of payment.

The focus in dealing with extortionate credit has been primarily on the interest rate when it may often be other terms and conditions of an agreement or business practices which cause detriment.

This section considers the following options for giving consumers more accessible protection:-

- ❖ Allowing named third parties to bring actions on behalf of a borrower or group of borrowers e.g. OFT, consumer bodies.
- ❖ Enabling consumers to challenge the terms of an agreement or other detrimental practices other than through the courts.
- ❖ Providing the OFT with restitution powers to compensate consumers.
- ❖ Empowering the OFT and other 'qualified entities' to initiate proceedings for a declaration in the public interest that a particular credit transaction, or a particular aspect of a transaction, shall be deemed unfair. This would assist in developing precedent, effectively on a 'test case' basis. It would not however involve the OFT bringing actions 'on behalf of' a borrower.
- ❖ Making the Time Order provisions more effective for borrowers.

## **4.2 Issues**

### **4.2.1 Group claims**

At present a court can only consider the agreement of the particular debtor who has asked it to re-open the agreement. There is a need to consider whether in certain circumstances it should be possible to bring a group claim and, if so, who ought to be able to bring such claims.

There are already provisions in the Enterprise Act 2002 that enable claims for damages for breaches of competition law to be brought in a representative capacity by a specified body on behalf of a group of named individuals.

A similar approach could be used in certain circumstances for consumer credit but if as at present the extortionate credit provisions are to depend on individual circumstances it is difficult to see how such an approach could be employed.

However there may be a contract term or practice that applies to a number of agreements, and does not depend on individual factors. A failure to reduce rates in line with the market may be such an example. In these circumstances we consider it appropriate to enable a named third party to bring an action against a rogue lender.

In addition to this we propose giving the OFT and possibly other 'quantified entities' the power to seek a declaration in the public interest, which would assist in developing precedent, and may enable other borrowers to pursue their own claims for relief. It would also provide a basis for guidance, and for licensing action.

Finally we consider it reasonable that if an extortionate credit claim is brought there should be a report mechanism whereby the OFT is notified. In addition to this there could be a notification requirement on licensees. The collation of such information will enable the OFT to monitor lenders activity and their fitness to retain a license as well as enable the opportunity to establish a central record available to the public.

**Question 19: If third party action is restricted to specified bodies, what bodies should be allowed to bring actions?**

**Question 20: On what basis should a power to seek a declaration be available, and what bodies might become 'quantified entities'?**

**Question 21: Do you feel that there should be a reporting obligation placed on the courts and/or the licensee when claims are brought on the grounds of extortionate credit? If so should it be extended to include the reporting of other disputes and if so what ones?**

One of the recommendations in the OFT's 1991 report, and endorsed in the subsequent reports by Elaine Kempson and NACAB was to allow the courts to re-open a credit transaction of their own motion. At present, the Act requires that the debtor must make a request to the court. We do not propose to pursue this option. Judges considered that this would adversely affect their impartiality to consider the case or an appeal. In addition, there is an issue as to who would pay for the proceedings if a judge instigated the case. However, dependent on what alternative dispute resolution is adopted (see 4.2.2

below), an option would be to provide for judges to refer cases across to that body if they considered the agreement might be extortionate/unfair.

**Question 22: If a dispute resolution body is established in an appropriate format do you feel that judges should be able to refer a case for consideration?**

#### ***4.2.2 Dispute resolution***

In Melanie Johnson's anniversary progress report on Tackling loan sharks – and more! We outlined the possibility of an independent body for considering extortionate credit claims as an alternative to or in addition to the courts.

At present should a consumer wish to make a claim that the credit agreement is extortionate they can apply to the court but could be liable for potentially high costs. In addition there is likely to be a major imbalance between the lender's legal capabilities and those of the consumer.

We are concerned that consumers are daunted by the proposition of going to court with an extortionate credit claim, and therefore propose to enable consumers to challenge, extortionate credit agreements, unfair credit transactions, and make complaints about detrimental terms or practices through an alternative dispute resolution mechanism.

Whilst at this stage we are investigating the principles of this proposal rather than the detail there are a number of key factors that we are aiming to achieve: -

- ❖ A neutral party to act as a mediator in negotiations. This could include dealing with issues between money advisors and creditors on repayment plans.
- ❖ For cases to be heard by experts in the field of credit, who will be aware of the costs, risks and lending practices.
- ❖ Be able to consider all complaints but have a clear jurisdiction between the dispute resolution body and the courts.
- ❖ Be easily accessible to the most vulnerable consumers in terms of cost, limited liability and procedures.
- ❖ Ideally compulsory jurisdiction for all licensees.
- ❖ Have powers that are enforceable and binding on all parties, for example to amend agreements and award compensation.
- ❖ Allow actions to be taken by a third party on either an individual or representative basis.

However we are aware that in creating such a mechanism there are a number of priority issues such as funding that need to be addressed. This could be achieved by: -

- ❖ Funding from an element of the Consumer Credit licence fee; and/or
- ❖ A structured application fee based on a case-by-case basis, paid by both consumer and lender;
- ❖ Costs to be paid by the lender in all cases; or

❖ Costs to be allocated upon deliberation.

There are a number of ways of creating an alternative dispute resolution/consumer redress mechanism, such as:-

**Mediation:** A private and structured form of negotiation assisted by a third party the decision of which is not binding. There are no fixed procedures and the mediator may not necessarily be an expert in the field of consumer credit but it is less formal and of low cost.

**Ombudsman:** An informal process, which the consumer can use free of charge if the business does not resolve the complaint within a pre-set time. The ombudsman has specialist knowledge and can mediate, investigate and award compensation - on the basis of what is fair taking into account the law, any relevant code and good industry practice. If the consumer accepts the decision it may be binding on both parties or binding only on the lender. Appropriate information can be exchanged with the OFT to assist with monitoring/enforcement. Membership of the ombudsman scheme can be made compulsory for businesses. Using the existing Financial Ombudsman Service would increase 'visibility' to consumers, avoid confusion over which scheme had jurisdiction and provide economies of scale.

**Arbitration:** A formal, private and binding process where a dispute is resolved by the decision of a nominated third party expert in this field. The decision is binding and enforceable on both parties. Rules and procedures are flexible and can be tailor made for the consumer credit market. The process could include mediation and is confidential although information could be supplied to the OFT to enable enforcement action if it is felt to be appropriate. An arbitrator can consider issues on points of law as well as more general principles of fairness and can deal with all consumer credit grievances however unlike the ombudsman the arbitrator would not investigate complaints. Governed by statute an arbitrator can have extensive powers, which include the amendment of terms in an agreement. Arbitration is easily accessible to consumers with the possibility of restricting costs and in the event of a group of actions **one** arbitrator can arbitrate on a number of similar cases. A panel of specialist arbitrators can be formed to deal with consumer credit disputes. Members of the panel would be kept up-to-date with contemporary consumer credit issues through regular briefings and training.

We recognise that no one system will be capable of achieving all our objectives and during the coming months we will be undertaking more work and further consultation on this specific proposal but seek your initial views on the following questions:-

**Question 23:** Do you agree that there should be a dispute resolution mechanism, other than the courts for consumer credit cases?

**Question 24:** What are the most important ways in which such a mechanism should differ from the existing procedures?

**Question 25:** If there is to be a new mechanism, how should it relate to the court system? Should it be a precursor to the court, be a stage in the court process, or should it replace the court process?

**Question 26: What do you consider are the most important matters over which the dispute resolution body should have jurisdiction?**

**Question 27: What do you consider is the most effective method for funding a new mechanism?**

#### **4.2.3 Redress**

There may be circumstances where for example a rogue lender has been found to adopt a particularly unfair practice. Although the OFT can take licensing action there is currently no redress available to consumers who have lost out. Where cases came before an alternative dispute resolution process (see above), we envisage that the dispute resolution body would be able to determine appropriate redress for the consumer. Where that is not the case, we are considering giving powers to the OFT which will enable them to issue restitution orders to compensate the consumer. A similar model has been adopted by the FSA, where for mortgages, they are able to sanction consumer redress as well as issue conduct of business rules and associated guidance, subject to prior consultation and cost benefit analysis. The FSA has the power to compensate consumers using restitution orders which work in two ways:-

- Their standard disciplinary mechanisms (tribunal etc) can require an authorised firm to provide restitution to consumers affected by the firm's contravention. In this case, the firm has the responsibility for paying recompense directly to the affected consumers; or
- Apply to the courts for an Order to be made against any firm (i.e. they don't need to be authorised). In this case the recompense is paid over to the FSA, and they have responsibility for ensuring that it reaches the affected consumers.

**Question 28: Do you support the proposal to provide the OFT with powers to issue restitution orders as a means of compensating consumers? If not what alternative mechanisms do you suggest?**

#### **4.2.4 Limitation periods.**

The Limitation Act 1980 sets out the maximum periods during which an action may be brought; a borrower would not be able to bring an extortionate credit claim once the relevant period has expired. In relation to an extortionate credit claim, the limitation period to reopen an agreement to seek to recover any monies already paid is six years. If any other remedy is sought then the period is 12 years.

In Scotland, claims arising from a contract must generally be made within five years of the relevant obligation becoming enforceable (Prescription and Limitation (Scotland) Act 1973 section 6 and schedule 1). There is also a longstop period of twenty years for claims, which are not covered, by the five-year period (section 7). Opinions are sought on whether challenges to the fairness of consumer credit agreements should be permitted in Scotland for as long as the debt can still be enforced against the consumer.

Claims that agreements are extortionate have often been met with a defence by the lender that the claim is statute barred. In many cases it might be

several years after the agreement is entered into that the borrower seeks legal advice, and the lender taking legal action usually prompts this. However, it may then be too late for the borrower to challenge the agreement, as he is time barred from doing so.

We propose to allow claims to be made by a borrower for as long as the debt can still be enforced against the debtor.

**Question 29:** Do you agree that credit agreements should not be subjected to the current limitations period in respect of extortionate credit agreements? If not, please explain why.

**Question 30:** Should there be a period beyond the end of the agreement in which claims can be brought? If so what do you consider to be appropriate and why?

#### **4.2.5 Time Orders**

Section 129 of CCA enables the courts in certain circumstances, for example when a creditor takes steps to enforce an agreement or following the service of a default notice, to make an order giving time to a borrower to pay any monies being claimed. In conjunction with this the court can, under section 136, amend the terms of the agreement, if it is deemed just to do so for example, by: -

- ❖ Amending how long the loan will last; or
- ❖ Changing the interest rate payable.

It has been argued that a greater use of the Time Order provision in the Act should be made in appropriate circumstances.

Two recent court cases have added to the confusion as to whether sections 129 and 136 are intended for temporary relief or not and in what circumstances a court can vary the agreement. In the case of *Southern and District Finance v Barnes* (1995) the court decided that an order could only be made on account of temporary financial difficulties. However on the facts of the cases, which the court addressed, they granted long term orders, in one case over 15 years. In the case of *DGFT v First National Bank PLC* (2002) the decision did not overturn the earlier ruling but highlighted the anomalies in sections 129 and 136 and that they were not achieving the protection for borrowers that they were drafted to achieve. Lord Bingham who gave the leading judgement, agreed that in general, time orders extending over a very long period were best avoided but went on to say that “the broad language of section 129 should be so construed as to permit the county court to make such orders as seems to it just in all the circumstances”. This confusion needs to be addressed.

Another concern arises where there is a reduction in the monthly repayments by the borrower as a result of financial difficulties. The reduction could be due to arrears, an agreed repayment plan for a temporary period or an instalment payment order made by the court. In all these cases, unless the interest rate is reduced to reflect the lower monthly payment being made, then there will be an underpayment of monthly interest and the outstanding balance will rise. It

has been highlighted that the courts rarely refer to the time order provisions and routinely make suspended/instalment orders in respect of regulated agreements without any reference to sections 129 and 136. The situation is then exasperated, as borrowers might not be advised by the lender that there is a further liability due beyond the repayment obligations set out in the judgement.

At present the right to apply for a time order and the consequential provisions to amend the agreement are not adequately drawn to the borrowers attention (despite being referred to in the section 87 default notice and the court documents). Also a borrower can only apply for such an order where the lenders bring proceedings or after a default notice has been served.

We therefore propose the following reforms to encourage greater use of the provisions: -

- ❖ Make it clear that the court can issue a time order for whatever duration it deems appropriate taking all circumstances into account.
- ❖ Allow the borrower the right to apply for a time order **at any time** throughout the agreement.
- ❖ Require the borrower to be provided with better information about the use of time orders and the power the court has. The circumstances in which the various forms of relief can be obtained should be explained. This could be set out in both the default notice and court literature. The latter of these is controlled by the court service and we will be consulting with them to see what changes can be made.
- ❖ Amend the provisions to require the court to consider on each occasion that it grants an instalment order or time order, the relief available under section 136, which provides for the amendment of terms in the agreement. This may including adjusting the rate of interest to take into account any continuing liability for interest which is accruing and which is not provided for in the monthly payments which are the subject of the judgement and the relief.

In addition to the above the earlier proposals on improving transparency will ensure debtors are informed of the ongoing amount of interest if it is the creditors intention at some future date to seek payment of it.

**Question 31: Do you consider the proposed changes to the Time Order provisions will enable a greater use of the time order provisions; If not how do you feel the intended objectives of sections 129 -136 can be achieved?**

#### **4.2.6 Time Orders - Scotland**

It has been highlighted that there may be a lower take up of Time Orders in Scotland because lay representatives cannot represent their clients. The Sheriff Court Rules Council has indicated that, as the CCA makes no reference to lay representation for Time Order applications then, in accordance with the normal rules of Court, no lay representation can be allowed. This contrasts with the position under the Debtors (Scotland) Act

1987, which specifically allows lay representation when applications are made for Time to Pay Directions and Time to Pay Orders.

The Government believes that allowing lay representation in Scotland in relation to Time Order applications under the CCA would increase debtor protection, as it would allow debt counsellors and advice workers to make these applications on behalf of their clients. The Government therefore proposes to amend the Act to make it clear that lay representation should be allowed when applications for Time Orders are made.

**Question 32: Should the CCA be amended to allow lay representation when applications are made for time orders?**

There are a number of points raised about the role of the Sheriff Clerk in Scotland in relation to proceedings under the 1974 Act. The Scotland Office and the Scottish Executive will discuss these issues further with interested parties in Scotland.

### **4.3 Existing Agreements**

In implementing the proposals in this consultation we need to consider how existing agreements are affected particularly as there are agreements with many years still to run. When the Act first came into force the extortionate credit provisions were applied to existing agreements. The fundamental objective of the review of the Act is to improve consumer protection and some of the proposals relate to fairness, operating practices, and transparency; issues that should be being complied with already, so we see no reason why these cannot apply to all existing agreements.

However there are proposals that are more specific to the structure, terms and conditions of agreements and we feel that ensuring all agreements comply with new legislation after an agreed transitional period may be an acceptable solution.

**Question 33: Which of the proposals do you feel cannot apply to all agreements upon adoption of the revised legislation?**

**Question 34: What do you feel is a reasonable time period after any new regulation is adopted for all agreements to comply with any revised provisions? Are there any provisions, which should only be applied to new agreements concluded after the legislation comes into force?**

## 5. Summary of questions

**Question 1:** Do you agree that by amending the provisions of the Act as proposed above it will enable agreements to be more easily challenged as being extortionate in a way which balances the interests of borrowers and lenders appropriately?

**Question 2:** What factors do you consider should be taken into account in assessing whether or not a credit transaction is unfair? Is there a need for any further definition of “unfair credit transaction” either in the legislation or otherwise fleshed out in guidelines?

**Question 3:** Are there any reasons why the factors in section 138(2) – (5) should not be relevant during the full term of the loan, and if so why?

**Question 4:** Do you support the principle of removing the factors from primary legislation into secondary legislation? What are the pros and cons of each alternative?

**Question 5:** Given the above do you feel any additional provisions are required in the CCA to deal with unfair practices?

**Question 6:** Do you consider that controlling the cost of credit with specific provisions relating to interest rates should be used in the UK credit market; if so please explain the most appropriate mechanism and provide substantiated arguments to support your view?

**Question 7:** Which of the approaches outlined above requiring lenders to lend responsibly do you think would best meet the needs of consumers and business? Are there other alternative approaches which would be preferable and, if so, why?

**Question 8:** Do you agree that prohibiting the charging of interest on a compound basis would be a fair and effective control against the escalation of debts? If not, what alternative would you propose?

**Question 9:** Can you please provide an estimate of the cost implications of prohibiting interest being charged on a compound basis?

**Question 10:** Do you consider there should be any restrictions on the interest charged on arrears? If so in what way should it be limited?

**Question 11:** Similarly do you consider there should be any restriction on interest charged on charges and fees? If so in what way should it be limited?

**Question 12:** Should all charges/fees be subject to a restriction on the interest that can be charged or is there a case for some to be excluded? If so, what charges/fees should be excluded?

**Question 13:** What do you consider a fair and reasonable period to allow before interest can be charged on any charges imposed beyond the initial charge for credit?

**Question 14:** Do you consider redefining the extortionate credit terms of the Act as proposed in section 2.3.1 above is sufficient to ensure that charges on arrears cannot be levied at an unreasonably high level?

**Question 15:** If not, what alternative controls do you consider should be applied?

**Question 16:** Should lenders be permitted to make charges in certain circumstances or should all costs be absorbed into the interest rate?

**Question 17:** Do you consider that there is a need to specify in legislation the frequency and content of account information?

**Question 18:** What and how regularly should information be provided?

**Question 19:** If third party action is restricted to specified bodies, what bodies should be allowed to bring actions?

**Question 20:** On what basis should a power to seek a declaration be available, and what bodies might become 'quantified entities'?

**Question 21:** Do you feel that there should be a reporting obligation placed on the courts and/or the licensee when claims are brought on the grounds of extortionate credit? If so should it be extended to include the reporting of other disputes and if so what ones?

**Question 22:** If a dispute resolution body is established in an appropriate format do you feel that judges should be able to refer a case for consideration?

**Question 23:** Do you agree that there should be a new dispute resolution mechanism, other than the courts, for consumer credit cases?

**Question 24:** What are the most important ways in which the new mechanism should differ from the existing procedures?

**Question 25:** If there is to be a new mechanism, how should it relate to the court system? Should it be a precursor to the court, be a stage in the court process, or should it replace the court process?

**Question 26:** What do you consider are the most important matters over which the dispute resolution body should have jurisdiction?

**Question 27:** What do you consider is the most effective method for funding a new mechanism?

**Question 28:** Do you support the proposal to provide the OFT with powers to issue restitution orders as a means of compensating consumers? If not what alternative mechanisms do you suggest?

**Question 29:** Do you agree that credit agreements should not be subjected to the limitations period in respect of extortionate credit agreements? If not, please explain why.

**Question 30:** Should there be a period beyond the end of the agreement in which claims can be brought? If so what do you consider to be appropriate and why?

**Question 31:** Do you consider the proposed changes to the Time Order provisions will enable a greater use of the time order provisions; If not how do you feel the intended objectives of sections 129 -136 can be achieved?

**Question 32:** Should the CCA be amended to allow lay representation when applications are made for time orders?

**Question 33:** Which of the proposals do you feel cannot apply to all agreements upon adoption of the revised legislation?

**Question 34:** What do you feel is a reasonable time period after any new regulation is adopted for all agreements to comply with any revised provisions? Are there any provisions, which should only be applied to new agreements concluded after the legislation comes into force?

## **6. Compliance costs.**

No Regulatory Impact Assessment (RIA) has been made at this stage as this consultation document is exploring a number of options on a number of issues. It is therefore difficult for us to quantify the costs and benefits arising from each option. However, we would be grateful if respondents could consider the possible implications of the various proposals and provide us with information about compliance costs and benefits that would result from these

In addition to the specific questions it is important that we can evaluate any compliance costs arising from any of the options in this document. Please identify and quantify recurring and non-recurring costs and savings separately. Examples of recurring costs include the costs of extra administration, or materials. Non-recurring costs are costs such as one-off expenditure on materials, buildings and changes to computer systems.

To put the figures into perspective, please provide figures against estimates of new credit advanced and credit outstanding at the end of the most recent financial year for which information is available. If some costs and savings cannot be quantified but can be identified, please list them and give an indication of the importance you attach to them.

### **Small Business impact assessment:**

The Department pays particular attention to the impact of the options on small business. We request that if you are or represent small business please supply information about the estimated impact of these options.

# Annexes

## **ANNEX A Consultees Approached :**

### **CHARITABLE BODIES**

Age Concern  
The Campaign for Interest-free Money  
The Christian Council for Monetary Justice  
Church Action on Poverty - Debt on our Doorstep  
Church Action on Poverty North East - Debt on our Doorstep  
Church Action on Poverty Scotland - Debt on our Doorstep  
Community Development Finance Association  
Help The Aged  
Mary Ward Legal Centre  
National Council for Voluntary Organisations  
Prospect Community Housing  
Royal National Institute for the Blind  
SAFE  
Scottish Churches Parliamentary Office  
Teacher Support Network  
Zacchaeus Trust  
Church Action on Poverty - Debt on our Doorstep  
One Parent Families

### **CONSUMER ORGANISATIONS**

Birmingham Settlement  
Citizens Advice Scotland  
Community Finance solutions  
Consumers' Association  
Consumers' Association of Singapore  
East Bristol Advice Centre  
Federation of Information and Advice Centres  
Financial Services Consumer Panel  
General Consumer Council for Northern Ireland  
Gloucestershire Money Advice Service  
Institute of Consumer Affairs  
International Consumer Policy Bureau  
Money Advice Association  
Money Advice Scotland  
Money Advice Trust  
National Association of Bank & Insurance Customers  
National Association of Citizens Advice Bureaux  
National Association of Citizens Advice Bureaux (North Region)  
National Consumer Council  
The National Consumer Credit Federation  
National Consumers Federation  
National Debtline  
North West London Consumer Credit Group  
Salford Anti Poverty Unit

Salford Money Line  
Scottish Consumer Council  
Sheffield Citizens Advice Bureaux Debt Support Unit  
Welsh Consumer Council

**CREDIT & HIRE INDUSTRY ORGANISATIONS**

Association for Payment & Clearing Services  
Association of British Credit Unions Limited  
British Bankers Association  
British Cheque Cashers Association  
British Vehicle Rental & Leasing Association  
Building Societies Association  
The Committee of Scottish Clearing Bankers  
Construction Plant Hire Association  
Consumer Credit Association  
Consumer Credit Trade Association  
Corporation of Finance Brokers Limited  
Council of Mortgage Lenders  
Credit Card Research Group  
Credit Services Association  
Finance & Leasing Association  
Hire Association Europe  
Institute of Credit Management  
National Association of Mortgage Brokers & Advisers  
National Pawnbrokers Association

**CREDIT REFERENCE AGENCIES**

Callcredit PLC  
Credit Data & Marketing Services  
Dun & Bradstreet Limited  
Equifax Limited  
Experian Limited

**EUROPEAN COMMISSION/GOVERNMENT**

Bank of England  
Cabinet Office  
Charity Commission  
Commission for Racial Equality  
Department of Enterprise Trade & investment  
DTI, Small Business Service  
Equal Opportunities Commission  
European Commission – Directorate General XXIV  
Fiji Ministry of Commerce Business Development & Investment  
Guernsey Trading Standards  
House of Commons Library  
Lord Chancellor's Department  
The National Assembly for Wales  
National Audit Office  
Office of Fair Trading  
Office of the Information Commissioner  
Scotland Office  
Scottish Executive

HM Treasury  
United Kingdom Permanent Representation to the European Union  
Wales Office

### **JOURNALS**

The Big Issue South West  
Consumer Law Today  
Credit & Car Finance  
This is money  
TS Today

### **LEGAL PROFESSION & SIMILAR BODIES**

The Association Of District Judges  
The Association Of District Judges - Law & Procedure Sub-Committee  
Faculty of Advocates  
Financial Law Panel Limited  
Forum of Insurance Lawyers  
The General Council of the Bar  
Law Centres Federation  
Law Commission  
The Law Society  
The Law Society of Northern Ireland  
The Law Society of Scotland  
Scottish Law Commission  
The Sheriffs Association

### **LOCAL AUTHORITIES**

Aberdeenshire Council  
Bedford Library  
Birmingham City Council  
Blackpool Borough Council  
Blaenau Gwent Council  
Bournemouth Borough Council  
London Boroughs of Brent & Harrow Trading Standards  
London Borough of Bromley  
Bury Metropolitan Borough Council  
Coventry City Council  
London Borough of Croydon  
Cumbria County Council  
Dorset County Council  
London Borough of Ealing  
East Ayrshire Council  
East Dunbartonshire Council  
Essex County Council  
Gateshead Metropolitan Borough Council  
Glasgow City Council  
London Borough of Hammersmith & Fulham  
Hampshire County Council  
London Borough of Havering  
Hertfordshire County Council  
London Borough of Hounslow  
Inverclyde Council

Kent County Council  
Kingston upon Hull City Council  
Lancashire County Council  
Leeds Central Library  
Lincolnshire County Council  
North Lincolnshire Council  
Milton Keynes Council  
London Borough of Newham Social Regeneration Unit  
London Borough of Newham Trading Standards & Consumer Protection  
Northumberland Council  
Oxfordshire County Council  
Powys County Council  
St Helens Metropolitan Borough Council  
Sheffield City Council  
South Gloucestershire Council  
Stirling Council  
Stockport Metropolitan Borough Council  
Suffolk County Council  
Surrey County Council  
London Borough of Sutton  
Swindon Borough Council  
Tameside Metropolitan Borough Council  
Tees Valley Joint Strategy Unit  
Torbay Council  
Warrington Borough Council  
West Sussex County Council  
West Yorkshire Trading Standards  
Wiltshire County Council

**LOCAL AUTHORITY ASSOCIATIONS**

Association of Local Authorities in Northern Ireland  
Association of London Government  
Convention of Scottish Local Authorities  
Local Government Association  
Welsh Local Government Association

**OMBUDSMEN**

Financial Ombudsman Service Limited  
The Ombudsman for Estate Agents

**ORGANISATIONS REPRESENTING SMALL FIRMS**

Alliance of Independent Retailers & Businesses  
Association of Independent Businesses  
Federation of Small Businesses  
The Forum of Private Business  
The Independent Food Retailers Confederation  
London Personal Finance Association  
The Union of Independent Companies

**OTHER BODIES, BUSINESSES OR INDIVIDUALS**

All Flintshire Credit Union

Liz Bateman  
John Bone  
Matthew Brodrick  
Felix Budelmann  
Frank Card  
Michelle Casciaro  
Lee Chesterman  
Tony Cuddeford  
David Deacon  
Dominic Houston  
Peter Dunn  
Richard Eason  
Enigma Amystery  
Louise Evans  
Etta Farrell  
Geoffrey Fielder  
Pip Giddins  
Alan Gilliland  
Hugh Hercus  
Peter Hingston  
Lorraine Hull  
Richard Jones  
Richard Jones  
Craig Kennedy  
Richard Mason  
Paul Matthews  
Joseph McAdam  
John Morrison  
The Mortgage Group  
Nationwide Trust Limited  
S Owens  
Gurinda Sandhu  
Paul Seviour  
Tim Sewell  
Barbara Seymour  
Duncan Smith  
Societe Generale  
Terry Arch Mortgage Services  
Andy Thompson  
Jane Wiltshire

**OTHER ORGANISATIONS OR BODIES REPRESENTING BUSINESS**

Association of British Insurers

Association of Convenience Stores  
The British Chambers of Commerce  
British Hardware & Housewares Manufacturers' Association  
British Insurance Brokers Association  
British Retail Consortium  
Confederation of British Industry

Direct Marketing Association (UK) Limited  
Dudley Sandwell Chamber of Commerce  
House Builders Federation  
Incorporated Society of British Advertisers  
Institute of Directors  
The Institute of Management  
Institute of Practitioners in Advertising  
The Mail Order Traders Association  
The Newspaper Society  
The Radio Advertising Bureau  
Retail Motor Industry Federation  
Scottish Grocers Federation  
Scottish Motor Trade Association  
The Society of London Theatre  
Society of Motor Manufacturers & Traders Limited  
Wine & Spirit Association of Great Britain & Northern Ireland

**REGULATORY OR SUPERVISORY BODIES**

The Advertising Standards Authority Limited  
Broadcast Advertising Clearance Centre  
Committee of Advertising Practice  
Direct Mail Services Standards Board  
Finance Industry Standards Association  
The Financial Services Authority  
Independent Committee for the Supervision of Standards of Telephone  
Information Services  
Independent Television Commission  
Office for the Regulation of Electricity & Gas (Northern Ireland)  
Office of Gas & Electricity Markets  
The Radio Advertising Clearance Centre  
The Radio Authority

**TRADING STANDARDS**

Local Authorities Co-ordinators of Regulatory Services  
London Trading Standards Authorities  
Trading Standards Institute  
Association of British Insurers  
Farrar & Co  
Masons  
McGregor Donald  
Francis Miller

## ANNEX B The Consultation Criteria

- 1. Timing of consultation should be built into the planning process for a policy (including legislation) or service from the start, so that it has the best prospect of improving the proposals concerned, and so that sufficient time is left for it at each stage.*
- 2. It should be clear who is being consulted, about what questions, in what timescale and for what purpose.*
- 3. A consultation document should be as simple and concise as possible. It should include a summary, in two pages at most, of the main questions it seeks views on. It should make it as easy as possible for readers to respond, make contact or complain.*
- 4. Documents should be made widely available, with the fullest use of electronic means (though not to the exclusion of others) and effectively drawn to the attention of all interested groups and individuals.*
- 5. Sufficient time should be allowed for considered responses from all groups with an interest. Twelve weeks should be the standard minimum period for a consultation*
- 6. Responses should be carefully and open-mindedly analysed, and the results made widely available, with an account of the views expressed, and the reasons for decisions finally taken.*
- 7. Departments should monitor and evaluate consultations, designating a consultation co-ordinator who will ensure the lessons are disseminated.*

*The complete code is available on the Cabinet Office's web site, address [www.cabinet-office.gov.uk/servicefirst/index/consultation.htm](http://www.cabinet-office.gov.uk/servicefirst/index/consultation.htm).*

### **COMMENTS OR COMPLAINTS**

If you wish to comment on the conduct of this consultation or make a complaint about the way this consultation has been conducted, please write to Mr P Martin, DTI Consultation Co-ordinator, Room 550, 1 Victoria Street, London SW1H 0ET or telephone him on 020 7215 6509 or **mail to:**  
[Philip.Martin@dti.gov.uk](mailto:Philip.Martin@dti.gov.uk)

## **ANNEX C Summary of 'Unjust Credit Transactions'**

### **A report by the DGFT on the provisions of Sections 137 – 140 of the Consumer Credit Act 1974**

#### **Terms of reference**

1.1 In November 1990 I was asked by the Parliamentary Under Secretary of State for Industry & Consumer Affairs, Mr Edward Leigh MP, to undertake a review of the existing provisions of the Consumer Credit Act 1974 ('the Act') for dealing with extortionate credit bargains, and to report on what, if any, reforms were needed to improve these arrangements.

1.2 This is the first review of these provisions, which are contained in sections 137-140 of the Act, since they came into effect in May 1977. In 1971 the Crowther Committee report on Consumer Credit had expressed the conclusion that there was a level of credit costs 'above which it become socially harmful to make loans available'. In a speech in October 1990, I argued that this view remained valid, but that a fresh look was needed at the arrangements. This review's principal aim has been to consider whether the existing provisions effectively deter, and provide relief from, credit arrangements which are socially harmful, or if changes are necessary to achieve such an objective.

#### **Conduct of the review**

1.3 The Office consulted widely during the course of this review. On 7 February 1991 I wrote to over 130 bodies including consumer organisations, credit industry trade associations, Government departments, independent legal practitioners and academics with specialist interest in credit. This consultation letter sought views on a number of issues including:

- i the nature and extent of the 'extortionate' credit problem;
- ii the effectiveness of the current provisions;
- iii any proposals for change, including:
  - amendments to tighten up the current provisions;
  - other proposals to supplement the current provisions; or
  - whether an entirely different approach to the problem was needed.

The Office received 59 replies to the letter, and I am grateful to respondents for their helpful and detailed comments, clearly involving much time and effort, which have been taken fully into account during the preparation of this report. A full list of those who replied is given at Annex F.

1.4 The Office also reviewed, and has drawn upon, legislation in other countries. Here again, I am grateful for assistance received from overseas officials and contacts. A summary of legislation in a number of overseas countries is set out in Annex E.

### **Summary of main conclusions**

1.5 Most credit, for most consumers, most of the time, causes no problems. But there is continuing concern about a minority of activities, mainly on the margins of the market, which can be described as socially harmful lending. By this is meant transactions where the costs of credit (in terms of price and the associated terms and conditions) substantially exceed levels which would be generated by a fully competitive market and/or are so oppressive or exploitive that no sensible person, independently advised, would find them persuaded – that borrowing, or further borrowing, is the solution to their financial difficulties. Such borrowers, often on low incomes, may face a limited choice of lender and have little, or no, bargaining power. They may be faced with anti-competitive, misleading or oppressive practices, especially those that obscure the terms and conditions of loans.

1.6 There is particular concern about abuses affecting the secured lending market where ‘non-status’ borrowers – those with poor credit worthiness – are induced to borrow on excessive or oppressive terms against the security of their homes without regard to their ability to repay the loan. With unsecured loans, the Office’s principal concern is with ‘rolling-over’ or ‘topping-up’ arrangements where a series of short-term cash loans, each one usually paying off existing indebtedness to the same lender, can trap borrowers (and sometimes several borrowers in the same household) into extremely expensive cycles of debt. A number of cases involving high APRs (annual percentage rate of the total charge for credit) have been drawn to the Office’s attention. While these remain of concern and are a factor to be taken into account, high APRs alone do not necessarily indicate socially harmful lending. At the more general level, the report identifies examples of practices, affecting both secured and unsecured lending which – in isolation or in combination – call for intervention. Intervention may involve reopening a transaction and providing relief to the particular borrower and/or the taking of steps to deter or prohibit unacceptable lending practices or terms and remove offenders from the market. It is desirable to strive for maximum consistency between these two strands of control and liaison between those concerned with their enforcement.

1.7 The extortionate credit bargain provisions of the Act have not effectively dealt with the problems to which they were addressed. There have been very few cases in the courts indeed and, in most of those cases, which have reached the courts, a restrictive interpretation of the provisions has been adopted. The provisions are not aligned with the consumer credit licensing regime. It is not certain whether the power to reopen a credit bargain extends to various abuses, which are to be found on the margins of the market, so that there may be no relief for the borrower. In any event the courts and commentators have tended to focus on the first leg of the statutory definition of an extortionate credit bargain (grossly exorbitant payments), rather than the

second leg – the untested concept of ‘grossly contravenes the ordinary principles of fair dealing’.

1.8 This reports analyses the substantive and procedural deficiencies of the existing law and sets out the principles, which have guided the Office’s proposals.

## 1.9 Recommendations

1 The Government should introduce legislation to reform and develop sections 137-140 of the Consumer Credit Act, re-casting them with a view to making them work as originally intended. The concept of an **‘unjust credit transaction’** should replace that of an ‘extortionate credit bargain’. In such cases the court would, as now, have the power to reopen an agreement, on application by the debtor (or surety), so as to do justice between the parties.

2 A finding that a transaction involved excessive – not grossly exorbitant – payments should be a factor in determining whether the transaction was unjust.

3 A new test of whether the transaction involved business activity which was deceitful or oppressive or otherwise unfair or improper (whether unlawful or not) – using the same statutory wording as is used to assess the fitness of a trader to hold a credit licence – should be a further factor in determining whether a transaction was unjust.

4 The other factors to be taken into account should remain as they are, but with one addition – ‘the lender’s care and responsibility in making the loan, including steps taken to find out and check the borrower’s credit-worthiness and ability to meet the full terms of the agreement’.

5 The court should be empowered to re-open a credit transaction of it’s own motion. It should also be stated explicitly that this would apply to defended and undefended cases.

6. The court should be required to notify the Director General of each case where a credit transaction has been found to be unjust.

7 The Director General and local authority trading standards departments should be empowered to initiate proceedings for a declaration that a particular credit transaction or any particular aspect of it shall be deemed unjust. Such power should be exercisable only in the public interest.

8 Tougher penalties should be introduced for the unlicensed (ie illegal) provision of credit.

1.10 In addition, the Office intends to:

1 give more publicity to consumers’ rights to have a credit transaction re-opened by the court;

- 2 encourage those with evidence about lending which appears to be unjust to bring it to the attention of the Office or local authority trading standards departments;
- 3 publicise practices, which it has found, in the course of its licensing activities, to be deceitful or oppressive, or otherwise unfair or improper;
- 4 draw the attention of the Government to comments received about the need for improvements in the access to alternative forms of credit for low-income consumers.

### **Impact of the recommendations**

1.11 The twin objects of these recommendations and proposed action by the Office are to deter socially harmful lending more strongly and to improve the ability of borrowers who are its victims to gain redress. The available evidence indicates that such lending, serious though its effects are, is a marginal activity. The vast majority of the credit industry who lend responsibly, and their customers, are not the target of the proposals in this report.

1.12 For the minority, I believe that the combined effect of the proposals will be to

Improve credit traders' behaviour and to reduce the incidence of such lending. There may well be an increase in the number of cases brought before the courts since one purpose of the proposals is to make it easier for debtors and their advisers to do so. I would not, however, expect this to lead to an upsurge of vexatious or unmeritorious cases, particularly as judgements emerge which give clear guidance from the courts about those aspects of credit transactions, which justify their reopening. Nor would I expect that the need for a minority to alter their methods and behaviour – so as not to enter into unjust credit transactions – will result in any significant increase in their costs passed on to borrowers. Overall, I believe the outcome will be beneficial to consumers and to the credit industry in weeding out unjust lending.

**Sir Gordon Borrie QC**  
**Director General of Fair Trading**

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