



Department of Trade and Industry
Consumer and Competition Policy Directorate

Tackling loan sharks – and more!

**A summary of responses to
the DTI's consultation on
financial limits and exempt
agreements of the Consumer
Credit Act 1974**

November 2002

A summary of responses to the DTI's consultation on Financial Limits and Exempt Agreements of the Consumer Credit Act 1974

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1. MINISTERIAL FOREWORD

In July 2001 I published a consultation document *Tackling loan sharks – and more!* which set out proposals for the first major review of our consumer credit laws in almost 30 years.

Six priority areas for reform were identified: -

- Bringing more credit agreements within the regulatory regime by increasing or removing the Consumer Credit Act financial limit and reducing the number of exempt agreements
- Changing the consumer credit licensing regime to target enforcement on keeping loan sharks out of the market.
- Making protection against extortionate credit more effective
- Enabling consumers to conclude credit agreements on-line
- Simplifying the advertising regulations
- Amending the early settlement regulations to give consumers a fairer deal
- Implementing the recommendations made by the Task Force on tackling overindebtedness

In March of this year I published a consultation on the first of these issues; to review the financial limits and the exemptions of the Consumer Credit Act.

We received more than 50 responses to our consultation and I am very grateful to everyone who took the time to comment. In summary the responses pointed towards:-

- Either a significant increase or removal of the financial limit
- Most business lending to be removed from the Act, though retaining protection for small businesses
- Retaining the existing exemptions

The consultation has been of great value and given me a firm basis on which to move ahead.

In view of the European Commission's recently published proposal to remove the financial limit from the Consumer Credit Directive and a similar approach in the recently agreed directive on the Distance Marketing of Consumer Financial Services, I have decided to proceed with the removal of the limit in the CCA.

When I launched the review of the CCA last year I stated my intent to tackle loan sharks that prey on vulnerable consumers. Removing the financial limit will not only bring more consumer borrowing within the scope of the Act, but also deliver the first of my actions to provide effective protection for consumers against loan sharks.

However, I recognise that removing the financial limit will bring a considerable increase in the amount of business lending caught by the Act. Consultees were strongly in support of maintaining the Act's protection for sole traders, small partnerships and other unincorporated bodies, but not for larger partnerships. Therefore I propose to amend the scope of the Act at the same time as removing the financial limit so that partnerships are only covered where there are three or less partners. We will start the process to make any legislative changes early 2003 prior to which some further work on the ancillary issues raised by consultees would have been concluded.

Finally given the clear message from consultees on retaining the current exemptions I propose to take no action here until the proposals on exemptions under a revised Consumer Credit Directive are much clearer. However, when FSA regulation of mortgages begins in 2004, most mortgages will be "carved-out" of the Consumer Credit Act. To the extent that the existing exemptions also cover second charge secured loans, we will want to look at how we should change these to ensure that the CCA regulates all the loans we want it too.

This marks the start in delivering a modern regulatory framework that promotes competition and choice for consumers within an appropriate level of protection for the 21st century.

Melanie Johnson MP
Parliamentary Under Secretary of State
For Competition, Consumers and Markets
Department of Trade and Industry

2. EXECUTIVE SUMMARY

We published our consultation paper in March 2002 to seek views on a range of options for: -

- Increasing/removing the financial limit for credit agreements regulated by the Act
- Re-defining or excluding business lending caught by the Act, and
- Reducing the categories of agreement exempted from the Act

These options would increase consumer protection by bringing more credit agreements within the regulatory regime. They also reflect the approach proposed in the European Union, where the Commission is looking to increase consumer protection under the Consumer Credit Directive by removing its financial limit and reducing the current exemptions.

[If reading this on line click here to go to a copy of the Consumer Credit Directive](#)

While the FSA will regulate first charge mortgages there will still be some lending secured on homes that will not be covered by FSA regulation or, because of the exemptions in it, the current Consumer Credit Act. We therefore sought views on raising or removing the current financial limit of £25,000 for consumer credit agreements to ensure most, if not all, consumer borrowing is regulated. At the same time we wanted to explore whether any increase should continue to include business lending and whether the existing exemptions should still apply.

We received 55 responses from a wide range of lenders, consumer groups and other interested parties. The main outcomes were:-

- 99% supported either an increase in or removal of the financial limit, although many lenders made this conditional on reducing or removing business lending from the Act and addressing some ancillary issues.
- 62% supported redefining business lending covered by the Act, with 50% supporting its complete removal.
- 71% supported the retention of the current exemptions under the Act, with only 7% advocating their removal.
- The majority of consultees favoured retaining the current exemption of agreements involving four payments or less in a period not exceeding 12 months.

51% of respondees supported a review of ancillary issues that could be affected by an increase in the financial limit. These included early

termination, unenforceable agreements and cooling off periods. Work will continue on these issues for the remainder of this year before any decision is taken as to whether any changes should be made.

The recently published European Directives for both Consumer Credit and the Distance Marketing of Consumer Financial Services have no upper financial limit and we will therefore seek to move to a similar approach for the CCA. If during the course of negotiations on the Consumer Credit Directive it is decided that a limit should apply we will adjust our proposal accordingly.

It is recognised that simply removing the financial limit would bring a considerable increase in the amount of business lending caught by the Act. Consultees were strongly in support of maintaining the Act's protection for sole traders, small partnerships and other unincorporated bodies, but not for larger partnerships. We will therefore start work on amending the scope of the Act at the same time as removing the limit so that for partnerships only those of up to and including three partners retain the protection of the Act.

Finally given the clear message from consultees on retaining the current exemptions we do not propose to undertake any changes here until the proposals on exemptions under a revised Consumer Credit Directive are much clearer.

3. ANALYSIS OF RESPONSES

The consultation paper was published on 28th March 2002 and was sent to a wide range of lenders, trade associations, consumer bodies, regulatory and Government bodies plus other interested parties.

3.1 Breakdown of Business

In total 55 responses were received, the breakdown of which is shown below.

- Consumer organisations – 7
- Trade Association/bodies – 8
- Regulatory/Supervisory bodies – 5
- Trading Standards – 5
- Lenders – 16
- Small business representatives – 3
- Government Departments - 3
- Others – 8

3.2 Financial Limits.

The consultation sought views on whether the financial limit should be increased or removed and whether there should be a financial limit for unsecured loans and no limit for 2nd charge mortgages.

Overall 99% of consultees supported an increase or removal of the financial limit. There were, however, a number of different opinions as to what a revised limit should be, with only two responses suggesting that the limit remain unchanged. 55% wanted a removal of the limit, but the majority of these made this conditional on removing business lending from the Act and amending some ancillary issues. The remaining respondents suggested revised limits ranging from £30,000 to £500,000 with £50,000 being the most popular. There was little support for multiple financial limits, on the grounds that it over complicated matters.

The arguments put forward for the removal of the limit were;

- Unless the limit is significantly increased lenders will continue to offer loans at £1 above the regulated amount so as to avoid having to comply with the Act. As a result some genuine consumer borrowing will be excluded from regulation.
- To incorporate all second charge lending the limit would need to be increased to a level that negated the need for a ceiling.
- Any ceiling requires regular review to take account of inflation and changes in market conditions.

- All consumer borrowing should receive the protection of the Act
- It reflects the proposal in the European Commission draft directive on consumer credit.

In addition to the above and as a result of the proposed scope of both the Consumer Credit and the Distance Marketing of Consumer Financial Services directives, where there will be no limit, we will seek to move to a similar approach for the CCA. However, if during the course of negotiations on the Consumer Credit Directive it is decided that a limit should apply we will adjust our proposal accordingly.

3.3 Business Lending

The current definition in the Act regulates loan/hire agreements made to individuals - including a partnership or other unincorporated body of persons not consisting entirely of bodies corporate. This extends the Act beyond 'natural persons' or 'consumers' and includes large partnerships. The consultation asked whether on not business lending should be re-defined or removed entirely from the Act.

50% of all consultees argued that business lending should be removed entirely from the scope of the Act. Most of these considered the CCA as the wrong vehicle for regulation of business lending, as it restricted the access of business to credit facilities. There was also concern as to the significant increase in business lending that would come under the scope of the Act through an increase or removal of the financial limit.

However a similar proportion of consultees argued that some categories of business should retain the protection of the Act, with 62% of these supporting a revised definition. The favoured option was to retain protection for sole traders, unincorporated bodies and partnerships up to and including three partners. There was strong opposition to any definition of 'business' being based on a monetary measure, e.g. turnover, VAT thresholds, etc.

A benefit of the current regime is that many business start-ups and small unincorporated businesses, which may not have ready access to financial advice, are protected by statute. This was recognised by the Small Business Service who advocated some retention of business lending within the scope of the Act. However they supported a revision of the definition, to exclude larger partnerships as it was felt that these would have access to appropriate financial advice.

There was an acknowledgment from all sides that small businesses can be just as vulnerable as a normal consumer, but it was also argued that the requirements of the Act impose procedures and protection that can hinder or be inappropriate for business lending. These can delay and

increase the cost of providing credit to business and even restrict its availability to such borrowers.

Some consultees supplied figures on the impact of any legislative change. The Finance and Leasing Association indicated that during 2001 25.4% of its total credit granted was to the business sector. Of this business lending over 92% was unsecured and below £25,000, with 59% being offered to sole traders, 13% to unincorporated bodies and 26% to partnerships (number of partners undisclosed). 2% was undisclosed. These same figures indicated that there was no secured lending to unincorporated bodies in excess of £50,000. The BBA indicated that just over 64% of the industry's lending to small businesses is for loans of less than £25,000.

It is recognised that increasing the financial limit will bring a considerable increase in the amount of business lending caught by the Act, although consultees were strongly in support of maintaining the Act's protection for sole traders, small partnerships and other unincorporated businesses. Therefore, we propose to amend the scope of the Act at the same time as increasing the limit so that only those partnerships of up to and including three partners are covered. We will bring forward proposals for legislation to achieve this at the beginning of 2003 once we have concluded our review on the ancillary issues that are highlighted below.

3.4 Related Issues

The consultation highlighted a number of potential issues arising should the financial limit be increased or removed without also changing certain ancillary provisions. We therefore sought views on any other provisions in the Act that would require further consideration if the financial limit is increased significantly. Over 50% of consultees supported a review of the following provisions:

- Early termination of hire purchase and conditional sale agreements
- Enforcement Orders; and
- Cancellation and cooling off periods.

Not surprisingly there was a balanced response to the **early termination** provisions with lenders being very concerned as to their increased exposure should limits increase and consumer representatives feeling that this was a very important consumer protection provision. Specific examples of increased risk to lenders were decreases in the value of second hand cars and computer equipment.

With regards to **Enforcement orders** lenders expressed their concern that any increase in the financial limits would increase their exposure

should the agreement be unenforceable due to what they deemed to be a small technical error. The issue was highlighted as a result of recent court decisions which lenders said had created concern and uncertainty for them.

It was suggested that full discretion should be given to the courts to enforce improperly executed agreements. There was strong pressure that these provisions be reviewed regardless of the House of Lords decision with regard to the case of *Wilson v First County Trust*. However we have concluded that any consideration of changes should not take place before the outcome of the House of Lords case is known.

The other key issue, referred to by over 50% of consultees, related to cancellation and cooling off periods. Again not surprisingly, there was a very balanced opinion depending on whom the respondees represented.

Finally some consultees again raised issues identified in the main *Tackling Loan Sharks* consultation. These included multiple and variation of agreements and joint and several liabilities, and as stated we propose to look at these during the remainder of this year before deciding on any action.

3.5 Exemptions from the Consumer Credit Act

Some categories of credit and hire agreements were originally exempted from the Act where alternative safeguards already existed or where to impose regulation was not in the interests of consumers. The main areas of exemption are:

- Mortgage lending
- Low-cost credit
- Short-term trade credit
- Overseas finance
- Certain land transactions.
- Insurance policies connected to exempt mortgages
- Overdrafts

The European Commission's proposal for a revised CCD seeks to reduce the number of exemptions and in this context consultees were asked whether any of the existing exemptions be retained, revoked or modified.

There was a commonality amongst the consultees that exemptions should be kept to a minimum; although no evidence was offered that the current exemptions have caused any detriment to the consumer or to

business. Only 7% advocated the complete removal of all the exemptions, whilst 71% suggested that they be amended. The remainder offered no comment. Consumer groups advocated that if the lending is **secured** and not covered by the FSA it should **always** be regulated. There were four main themes from the responses: -

- Over 50% supported overdrafts losing their exemption on advertising, in particular so that APRs are quoted, but 82% supported the status quo regarding exemption from documentation requirements
- 28% supported the exemption for short term credit being restricted to only those agreements where no interest was applied
- The majority of respondents favoured retaining the current exemption on loans with four payments or less over a 12-month period.
- 11 respondents supported extending the current exemption for the utility companies to include telephone and television service providers and the essential hiring of equipment/metering equipment supplied by the service provider. No substantive objections were received to this proposal.

These issues are covered in greater detail following the specific questions below.

3.5.1 Mortgage lending

In response to requesting views on who should regulate 1st charge mortgages there was no support for those 1st charge loans not regulated by the FSA to be brought within the scope of the Consumer Credit Act, although 22% of respondents wanted **all** secured lending to be regulated by the FSA.

The only 1st charge loans highlighted that could potentially be unregulated as a result of this approach related to 'Buy to Let' (BTL) mortgages. 80% of those that had a view felt that BTL's were commercial loans and should not be regulated by the CCA.

We then sought views on whether any loans secured by 2nd charges on property would remain unregulated if the financial limit were increased without some modification to the exemptions for mortgage lending. The responses identified no such loans, other than those already exempted from the Act. We will therefore need to look at how the exemptions should be amended to ensure that all second charge loans are regulated under the CCA. However the Building Societies argued for equal treatment with the banks with regards to their subsidiaries having automatic exemption for some types of secured lending from the Act. We do need to revisit this exemption in the light of the prospect of FSA

mortgage regulation but it may be that once first-charge mortgage loans are carved out of the CCA, this will no longer be an issue. As we are looking to regulate all 2nd charge lending we will be looking at this issue along with the other ancillary issues.

3.5.2 Low-cost credit

With regard to the exemption related to low-cost credit we asked if non-commercial low-cost loans should remain exempt on the grounds that there is no perceived consumer detriment.

An overwhelming 80% of consultees supported the continued inclusion of this exemption in its current definition. Of those that petitioned for the exemption to be removed the main concern was that although the rate may be low there may still be unduly onerous terms and conditions.

With regards to Credit Unions it was generally acknowledged that they provide a valuable service to those on low incomes and help to reduce social exclusion. Whilst they are regulated by the FSA it was felt that there is little to be gained by subjecting them to the CCA's regime as well.

3.5.3 Short-term trade credit

With regard to short-term trade credit we asked if the number of repayments should be further restricted to qualify for exemption and whether these exemptions should be restricted to those agreements where there is no interest charge.

In total there were 34 responses on this subject with 45% advocating change to the current exemption. From the consumer representatives there was a general feeling that the current limit of four payments in a 12-month period was being abused and it meant that lenders did not have to quote the APR on such agreements. As a result it did not enable the consumer to shop around. Industry argued to retain the existing exemption as it was felt it had caused no consumer detriment. The main focus related to the facility to pay insurance premiums and other mortgage related charges over 4 payments. Many lenders currently debit annual insurance premiums to the mortgage account each year and the borrower repays this over the course of that year.

Of those that supported change nearly 80 % proposed one payment within a three-month period. It was suggested that the exemption should be aimed at short-term credit where there is normally no interest or other charges, or those limited to set up or administration charges. Having noted the split in the arguments over retaining the current exemption we have decided to take no further action until we are clearer on the

European Commission's intent on exemptions in the Consumer Credit Directive.

There was also support from 10% of respondents, mostly consumer groups, to bring charge cards within the scope of the Act to ensure consumers get more protection. It was indicated that 50% of the 'payment-card' market is now made up of debit cards and therefore this significant sector of this market is unregulated

However, given that debit cards are primarily a method of payment, similar to cheques, rather than a vehicle for the granting of credit and there is protection for consumers under the Banking Code we do not consider it appropriate for them to be brought under the regulation of the Consumer Credit Act. However, charge card agreements are clearly a form of credit and are largely exempt from the Act because they fall within the number of payments exemption outlined above. We will look at charge cards in the context of our consideration of whether it is necessary to revise this exemption in the light of the EU proposal.

3.5.4 Overdrafts

The overdraft as a short-term credit facility is highly valued by consumers for its simplicity and easy access. This exemption differs from those listed above, as although the bulk of the Act applies to overdrafts they are largely exempt from Part V of the Act, which includes sections covering rights of cancellation and withdrawal, and documentary requirements. In addition, advertisements for overdrafts do not have to include a statement of the APR.

Although the debtor is given advance notice of the charges payable under an overdraft facility, the absence of the APR means it is difficult for him to compare overdrafts with other credit facilities. We therefore sought views on whether advertisements for overdrafts should quote an APR and should the exemption be limited further so overdrafts become subject to the Act's documentary requirements.

Overall 73% of respondents felt that overdrafts should quote an APR. Some lenders were not averse to this, as they already do so on a voluntary basis. Given that sectors of the industry already provide illustrative APRs for an overdraft and this would enable consumers to make better comparisons of this product, we will develop proposals for requiring APRs on overdrafts.

Although 18% supported the removal of the exemption on documentary requirements, it was widely acknowledged that this facility does enable consumers and small businesses to gain access to this form of credit at short notice. No evidence was supplied to indicate that the lack of

documentation caused any consumer detriment and so we do not propose to change this exemption.

3.6 Consumer Hire agreements

The Act also regulates consumer hire agreements which are capable of lasting more than three months and do not require the hirer to make payments of more than £25,000. This facilitates the short-term hire of goods at short notice with minimal documentation. The level of regulation is not identical to that for consumer credit agreements but the Act does contain provisions on the form and content of agreements, cancellation and termination rights and other matters.

Agreements for the hire of metering equipment used for the supply of gas, electricity and water are exempt from the Act. Metering equipment is technically hired to the customer, but it was considered onerous to require these utility companies to comply with the Act. There does not appear to be evidence of consumer detriment as a result of this practice so we sought views on extending this exemption to other utility providers, for example telephone and television service providers.

There were only 11 responses, from different groups on this particular area of the legislation, due principally to its specialist market. However over 90% of those responses agreed that the exemption should be extended and we will start looking at this proposal.

The consultation also sought views on whether there was a case for regulating more consumer hire agreements, either by increasing the upper financial limit for these agreements, changing the definition of a regulated consumer hire agreement, or revoking/modifying the existing exemption. Of the responses, 5 consultees supported the total removal of hire agreements from the CCA, primarily to harmonise the Act with the Consumer Credit Directive. The remainder felt that the present short term hire exemption for agreements of 3 months or less should remain.

Of those respondees that considered hire agreements should be regulated, the majority favoured keeping the increase in line with the overall financial limit of the Act. Figures supplied indicated that at present 70% of hire business to non-corporates is currently regulated and an increase in the financial limit to £50,000 would increase this to 95%. Over 90% of hire agreements were for business purposes, with nearly 50% to the sole trader.

It is therefore proposed to remove the financial limit for hire agreements so that it remains in line with the main financial limit of the Act. The re-defining of business lending will ensure that specific areas such as the plant hire business with the larger partnerships are not affected.

4.ANNEXES

ANNEX 1: LIST OF RESPONDENTS:

CONSUMER ORGANISATIONS

Church Action on poverty (Debt on our Doorstep)

Federation of Information Advice Centres

Financial Services Consumer Panel

Institute of Consumer Affairs

National Consumer Council

National Debtline

Scottish Consumer Council

CREDIT AND HIRE INDUSTRY ORGANISATIONS

Association for Payment & Clearing Services

British Bankers Association

British Cheque Cashers Association

British Vehicle Rental & Leasing Association

Consumer Credit Trade Association

Council of Mortgage Lenders

Institute of Credit Management

The National Consumer Credit Federation

GOVERNMENT

Small Business Service

Lord Chancellor's Department

HM Treasury

LEGAL PROFESSION AND SIMILAR BODIES

Association of District Judges

LOCAL AUTHORITY ASSOCIATIONS

Welsh Local Government Association

OMBUDSMEN

The Financial Ombudsman Service

ORGANISATIONS REPRESENTING SMALL FIRMS

Federation of Small Businesses

The Forum of Private Business

OTHER BODIES, BUSINESSES OR INDIVIDUALS

Abbey National PLC

Anthony Sharp Associates

Barclays Bank PLC

Berwin Leighton Paisner

Bob Imrie BA MTSI DMS DCA

British Telecom

Cheltenham & Gloucester PLC

Co-Operative Bank

Hrafnkell Tryggvason

JCB Finance Limited

Kensington Mortgage Company

Key Business Finance Corporation PLC

Kirklees Credit Union Forum

Nationwide Building Society

Norwich & Peterborough Building Society

Paragon Group

Portman Building Society

Professor Macleod – University of Liverpool

Royal Bank of Scotland

Skipton Building Society

Swift Advances PLC

University of Salford

Yorkshire Building Society

REGULATORY OR SUPERVISORY BODIES

Advertising Standards Authority

Finance Industry Standards Association

Office of Fair Trading

Radio Advertising Clearance Centre

TRADING STANDARDS

Glasgow City Council Trading Standards

Kent County Council Trading Standards

Trading Standards Institute

LACORS

London Trading Standards Association