StepChange Debt Charity response to Credit card market study: Consultation Paper CP17/43

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Introduction

StepChange Debt Charity is the largest specialist debt advice charity helping people across the UK. Demand for our services has increased to its highest level in the first half of 2017 when 326,639 people contacted StepChange Debt Charity for help and support with their problem debt.

We welcome the opportunity to respond to this consultation as credit cards are the most common type of debt held by our clients. In the first half of 2017, around two thirds of clients (67.2%) had one or more, with an average total credit card debt of £8,134.

Q1: Do you have any further comments on our amended proposals and the draft Handbook text in Appendix 1?

Communications at 18/27 months on CRA reporting

We welcome that the FCA recognises the concerns about the impact of references to CRA reporting in communications at the 18 and 27 month stages including that this could be perceived as a threat and cause undue alarm to consumers. However, there does not seem to be a major difference between the previous proposal of a warning and the change of making customers aware of the risk that card suspension could potentially be reported to a CRA. We are concerned that making customers aware of this potential impact could still be perceived as a threat to customers. It could still lead to the possibility of them making unaffordable repayments or borrowing from other sources to increase repayments and getting further into financial difficulty.

It is important that communications at the 18 and 27 month stages encourage customers to engage with firms. This must be done by ensuring customers get the right messages about the help available to them including signposting to free debt advice and forbearance if they are struggling with repayments. We would support the firms coming together to develop an agreed standard and form of words that is encouraging customers to seek help from them where appropriate. Customers should not feel that their only option is to increase repayments that may be unaffordable, in order to avoid reporting to a CRA.

Moreover, in cases where forbearance is granted, including a reduction in the interest rate, the customer may still be making higher than the contractual minimum payment. Therefore it would not be appropriate to report this to CRAs as a negative event as the customer would be paying more with forbearance than they did when they were paying the minimum payment.

The consultation paper states that it is for firms and CRAs to determine the circumstances that would lead to reporting to the CRAs and the content of that reporting. It is essential, nonetheless, that the industry and CRAs take a consistent approach to reporting in cases where the card is suspended and/or when forbearance is implemented. An inconsistent approach to this will be unfair and confusing to customers as they will be treated differently by different firms. We would urge the FCA to ensure that the industry and CRAs bring in consistent approach to reporting the CRAs when cards are suspended and to ensure this approach is fair, transparent and understandable for customers.

Referrals to debt counselling:

We accept that in order to be in line with other CONC rules, there has been amendment to the original proposals so that customers can refer to authorised debt advice firms that will charge customers. The messaging on this should give prominence to free debt advice and detail what the costs associated with using debt counselling services are. This would ensure customers can make an informed choice about where they turn for support with their debt problems.

Implementation period extended to 6 months:

We understand the reasons given for the extending the implementation period for firms to comply with the new rules 6 months after they come into force and accept that this may be a more practical timescale for firms.

We are however, concerned about those customers who have already been in persistent debt for over 18 months when firms have to comply with the rules. They may not benefit from the protections of the rules tackling persistent debt for an extended period. For example, those already at 36 months of being in persistent debt 6 months after the rules come into force, will only receive the 18 month information remedy. They will then not get the 36 month intervention until another 18 months has passed. This would mean it will be 54 months or 4.5 years before the usual 36 month intervention comes in. If these customers then are able to make sustainable repayments over a 4 year period then they will be in persistent debt for 8.5 years. This is clearly contrary to the original intention of the remedies to reduce the level and extent of persistent credit card debt. We would ask the FCA what the plan is for support to be given to this specific group.

We understand that it might not be appropriate to offer this group of customers the 36 month intervention straight away. They will not have had sufficient information or time to make an informed decision at this stage as they would not have been provided the earlier communications (e.g. at 18 months). The question is why it will be another 18 months before the 36 month intervention comes in for these customers. The FCA should develop a fast track approach for customers in these exceptional circumstances so they do not have to wait another 18 months before action is taken.

This group of customers who are have already been in persistent debt for over 18 months when the firms comply with the rules are likely to be more vulnerable to being in or falling into financial difficulties. Therefore the firms should be proactively identifying this group and monitoring closely if they are showing any signs of financial difficulty and need early intervention or forbearance.

This should also apply more broadly to all those customers in persistent debt at 18 months. The consultation paper states that there will not be any changes to the proposals on earlier intervention. In our response to CP17/10 we suggested that where people are in persistent debt for 18 months this should be treated as a sign of actual or potential financial difficulties. This would, as part of the early intervention proposals require firms to identify and monitor these customers more closely and take action where appropriate. We would ask therefore suggest the FCA consider including those that have been in persistent debt at 18 months to be include in monitoring for financial difficulties as part of the early intervention measures.

Extending the repayment period to over 4 years in exceptional circumstances

One of the proposed changes in this consultation paper is that in exceptional circumstances the repayment period can be extended beyond four years but that the extension should not be significant and there should be no additional cost to the customer as a result of this.

Our concern with this proposal is that it won't address the issue it is intended to tackle. In paragraph 2.33 of the consultation paper, it notes the concerns that some customers, especially those in vulnerable situations may feel pressured to accept unaffordable repayment plans. This is the justification for allowing an extension of over four year repayment periods in exceptional circumstances. However, the risk of customers feeling pressured to repay at levels they can't afford or borrow from other sources in order to not lose their credit card will still remain.

The remedies as currently structured create a 'cliff edge' at 36 months where customers essential have two options. One option is a repayment plan making higher repayments to pay off the debt with continued contractual interest payments. The other is forbearance that has wider consequences including having the card suspended and being reported to CRAs. The aim of allowing this extension period in exception circumstances is presumably to try to slightly alleviate this cliff edge and give people longer to repay without them been concerned about having their card suspended. However, this still leaves the central problem of there being potentially different treatment for people with different repayment characteristics.

There is currently no option for firms to think about what is the suitable product for customers, what is reasonable to charge them and to restructure the product so it can be affordable repaid without having to cancel use of the card completely and report this to CRAs. Moreover, in many cases customers will have been meeting the contractual terms of their credit agreement so should not be penalised, by being reported to CRAs, when they enter forbearance. This would mean a significant rethink of the remedies that we suggested in response to CP 17/10 but understand the FCA are not taking forward.

Another concern with this proposal for extended repayment periods in exceptional circumstances is that the rules as they are currently drafted [in CONC 6.7.33 G (2)] would allow firms in certain cases to extend the repayment period and make customers repay more rather than offer them adequate forbearance. Instead of extending the repayment period, lenders should be being encouraged to offer greater levels of forbearance at 36 months. This is because credit card customers at this three year point would already have paid more in interest on a credit card than they would have on a personal loan for an equivalent period. As the example below illustrates:

Example: A credit card with a £3,000 balance when it was taken out with a monthly borrowing rate on 1.456% (about 18% APR) a standard rate in 2017. The minimum repayment is 1% off balance plus interest accrued in a month.

- The interest accrued by 36 months on this card would be £1,326.

In comparison a £3,000 personal loan repaid in three years from a high street bank has the following interest:

- High street bank 1: £631 in interest (on a special deal)
- High street bank 2: £920
- High street bank 3: £1,057

36 month intervention:

- At 36 month if the credit card customer agrees to a pay down plan (with no forbearance/interest suppression) of 4 years. They will have paid £2,071 in interest over the full seven years since they took the card out.
- If they are offered forbearance including full interest rate suppression then they would save £745 as they would continue to have repaid £1,326 in interest rather than the £2,071.

In comparison, a £2,000 personal loan (equivalent to the credit card balance at 36 months of £2,089) repaid over 48 months (4 years) would be:

- High street bank 3: £2,000 personal loan repaid over 4 years: £962 in interest
- High street bank 2: £2,000 personal loan repaid over 4 years: £1,047 in interest

As the example illustrates, the credit card customer would have paid more in interest over the 36 months than for any of the comparable personal loans over the same period. It is therefore, reasonable to suggest that the credit card lenders have made sufficient profit from the credit card and should be offering forbearance including interest rate suppression to customers at this point.

Moreover, the interest paid on four year pay down plan with the credit card is not significantly less expensive the interest paid on a £2,000 personal loan repaid over four years. For example, comparing the £745 in interest payments over the four year pay down period with £962 in interest on the Barclay's loan or £1,047 on the Natwest loan. Therefore taking out a new loan to repay the debt would only be slightly more expensive in interest than repaying with a pay down plan.

The concern is that by allowing firms to ask customers to repay over five years rather than over four years then forbearance including full interest suppression is even less likely to be offered. Firms will not have strong incentives to offer the client further forbearance in these exceptional circumstance as they can follow the rules and offer a more profitable option (for the firm) to customers. The FCA findings from the Credit Card Market Study found that firms have few incentives to address customers with persistent debt as these customers are profitable.

If the aim of these remedies is to go some way to addressing the issues with firm incentives then this change in the rules provides a loophole. If there is no prescription on what type of forbearance has to be offered and no clear direction for what exceptional circumstances are. Then firms can use this new change in the rules to go extend the repayment term rather than offering additional forbearance (full interest suppression) and make more revenue from customers in persistent debt.

The FCA should provide further clarity on what it means by ‘exceptional circumstances’ and when these would occur. For example, would exceptional circumstances only mean where a customer cannot afford to repay the full balance in four years with an interest rate freeze. There also needs to be clarity about what period of time is being referred to in the extension. The guidance [CONC 6.7.33 G (2)] states that the ‘extension should not be significant’. However, this could mean 1 month, 6 months, one year or another 18 months. The FCA has been clear about the 3-4 year repayment period and needs to be similarly clear what a reasonable maximum period of extension would be.