BCCA

Competition Commission
Payday Lending Market Investigation
Statement of issues

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GENERAL COMMENTS AND OBSERVATIONS OF BCCA

We welcome the opportunity to provide our comments and observations to the Competition Commission ('CC') on the Statement of issues published by the CC on 14 August 2013.

Background

- BCCA is a trade association representing third party cheque cashers, short term unsecured lenders (high street and online), including payday lenders and credit brokers. The vast majority of our members are SME's.

- Our **high street members** are often family run businesses with one branch or a very small number within a localised area. They tend to offer multiple services to consumers which may include some or all of the following; third party cheque cashing, short term unsecured lending (including payday lending), foreign exchange, money transmission, pawnbroking, sale of new, used or second hand goods, sale and buy-back, log book loans, pre-paid cards.

- Our **online lender members** are typically start-up businesses and new entrants into the market. Our online members generally focus on providing short term loans.

Below we have cited the paragraph in the Statement of issues in italics. Our comments/ observations are underneath and they specifically refer to parts of the paragraph that we have highlighted in bold. Where there is no highlighting, our comments/ observations relate to the paragraph as a whole.

- ***Paragraph 10****. The demand for relatively small, unsecured short-term loans to meet temporary gaps in cash flow is not a new phenomenon and has long been a feature of people's formal and informal financial arrangements. However, what appears to be a relatively recent development, in the UK at least, is the development of companies primarily providing specific credit products to meet this demand. Payday lending is defined in our terms of reference as 'the provision of small-sum cash loans marketed on a short-term basis, not secured against collateral, including (but not limited to) loans repayable on the customer's next payday or at the end of the month and specifically excluding home credit loan agreements, credit cards, credit unions and overdrafts'. As noted in the OFT reference, the term payday loans is not used exclusively to refer to loans linked to the borrower's payday. For the purpose of this issues statement, and based on our initial research,* ***we consider payday loans to be unsecured loans which are generally taken out for less than 12 months, and where the amount borrowed is usually less than £1,000.***[4]

In our opinion, the breadth of scope of the inquiry as defined in Paragraph 10 (and highlighted) goes beyond the nature of the product referred to the CC for investigation.

- ***Paragraph 11****. The development of companies offering these loans appears to have originated abroad, particularly in the USA, from related services, such as cheque cashing. The USA experienced significant growth in the provision of payday loans from the 1990s though the growth in the UK has been more recent.*
  We note a number of the current larger providers in the UK are part of US companies and that some also operate in related businesses, such as pawnbroking.

  Payday loans have been available in Britain since 1997[1] and were often referred to as a 'payday advance.' They too grew out of third party cheque cashing.[2] We agree that payday lenders in the UK drew on the experiences in the United States where they have been available commercially since 1994, although the practices in the two countries differ in a number of significant ways.[3]

- ***Paragraph 28.****The CCA does not provide for restrictions on the interest rates payday loan companies can charge.* ***However, advertising of payday lending is subject to the Consumer Credit (Advertisements) Regulations 2004; this means that the 'typical APR' must be stated in all advertisements.***

  Most credit advertising must comply with The Consumer Credit (Advertisements) Regulations 2010 ('CCAR'). As a consequence of this legislation, it is now the 'Representative Example' that must be quoted in advertisements where required to under the CCAR. It is not necessarily required in all cases.

- ***Paragraph 39.*** *The OFT's compliance review found that the average value of a payday loan is between £265 and £270. It noted that loans were marketed to consumers as one-off short-term loans.* ***Assuming the loans were repaid on time, the OFT found that the costs were on average £25 per £100 borrowed for 30 days.***

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  In our experience, the range of pricing for payday loans varies and in many respects is dependent upon whether the loan is offered on the high street or online. Higher charges apply in the online space (when compared with high street lenders) and this is in part borne out of customer acquisition costs.

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[1] Information extracted from '*Pay Day Advances The companies and their customers'* – Nicola Dominy and Elaine Kempson Personal Finance Research Centre (2003) page 4.
[2] As above.
[3] As above.

We agree with the comment made in Paragraph 36 (when referencing the research conducted by the Personal Finance Research Centre at the University of Bristol) that *'the relative anonymity offered by an Internet-based service was a particular consideration for online payday loan customers.'*

- ***Paragraph 40.*** *The total cost to a customer of taking out a payday loan may depend on a number of factors including: the amount borrowed; the length of the loan; the lender's pricing policy, including the interest charged; whether the customer agrees to pay for a same-day transfer; and whether the customer is late with repayments. The different components added to the original loan (the principal) include interest, transmission fees, late payment fees, and other charges relating to the recovery of the principal.*

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  We would also like to add that the means by which consumers obtain a payday loan will also affect the total cost. For example, it is unlikely that lenders offering payday loans on the high street would apply same-day transfer charges, for example.

- ***Paragraph 43****. It appears from our initial observations that, regardless of whether they are sold online or in stores, the pricing of payday loans is not straightforward, potentially involving daily or monthly interest, fixed fees and charges for late payments.* ***We also note that, taken at face value, APRs are very high relative to other types of credit.*** *We will investigate further the extent to which these observations are accurate reflections of the industry.*

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  There is another area of the consumer credit market where the cost of credit is high (and consequently the APR would also be high if there was a requirement to quote) and that area is bank overdrafts. In our opinion pay day loans are the only true alternative. They are typically cheaper than virtually all "unauthorised" or "unapproved" overdrafts and they were developed for this reason[4]. We are not aware of any such overdrafts which are cheaper but there may be some. For example, one current account with a major bank has a "reserve" facility. This is, in reality, a £150 overdraft. The fee for dipping into this reserve, no matter by how much is a flat rate of £22 for up to five days, following which time the same fee is charged again.

  The lowest possible APR for this "loan" is 2,197,185.9% (i.e. just under 2.2 million %). This assumes the maximum £150 is borrowed for the full 5 days. In reality, the APR would be much larger and a better

[4] Information extracted from '*Pay Day Advances The companies and their customers'* – Nicola Dominy and Elaine Kempson Personal Finance Research Centre (2003) pages 4/5

assumption when calculating a representative APR would be for half the facility for about half the period - £75 over 3 days. In fact, the APR in this case is 3,903,377,926,060,990.00% (3,903 trillion %). You may like to check the calculations with the Department for Business, Innovation & Skills (BIS) or the Office of Fair Trading (OFT).

However, banks do not have to quote APRs for overdraft facilities linked to current accounts because of an exemption in the EU Consumer Credit Directive (ECCD), negotiated by the UK at the drafting stage following representations made by the banks. Furthermore, implementation of this opt-out is at the discretion of individual Member States. Needless to say, the UK did indeed decide to implement it, despite the objections of the short term lending industry which felt that all such loans should have to comply with the same regulatory conditions.

- ***Paragraph 46.*** *If we find that the characteristics and outcomes we identify are indicative that the market could be more competitive, we will consider what features of the market might be driving them. As described in our theories of harm (see below), these features may include impediments to customers' ability to search, switch and identify the best value product.* ***Another possibility is that there may be significant barriers to successful entry*** *or expansion, that, coupled with high concentration, mean that firms in the market enjoy significant market power.*

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Our members have found it challenging accessing merchant services from banks and/ or service providers. In many cases where members have been refused, banks have cited 'reputational risk' as being the reason why the service was declined.

Indeed when BCCA, as a small business applied for merchant facilities from an acquirer, we were initially turned down. It appeared that the credit risk team looked at our website and wrongly assumed that we were actually engaged in payday lending. Once that was found not to be the case, our application was successful

In our opinion, whilst we recognise that there is evidence within, for example, the OFT Payday Lending Compliance Final Report, which identifies compliance concerns, lenders should be judged on the merits of their application for merchant services rather than banks seemingly applying policies which preclude any applications from lenders in that sector being successful particularly given that payday lending is a regulated consumer credit product.

We recognise banks commercial freedom to decide who they offer accounts/ services to, but it should be carried out in a fair and transparent way so lenders are granted the same opportunities and applications are assessed on merit.

- ***Paragraph 72****. If significant barriers to entry or expansion exist, we would expect to see evidence of the existence of such barriers and limited examples of successful entry on any significant scale.* ***We will seek to understand whether there are barriers to successful entry or expansion.*** *In our assessment, we will consider issues including:*

  • *the role of advertising expenditure by large incumbents or other costs associated with gaining customers, such as acquiring leads from third parties;*

  • ***whether regulation represents a barrier****; and*

  • *the technology investment required.*

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- In relation to barriers to entry, please refer to our comments under Paragraph 46.

- In our experience, the current regulatory regime is not necessarily a barrier to entry. However, we do have concerns that the new regulatory framework under the Financial Conduct Authority (FCA) may have this effect. In our comments and observations to the FCA's consultation paper 13/7 published on 6 March we expressed our concerns that those currently in the market may exit. We stated the following (relevant competition related aspects detailed):

- **Proportionality** – It is absolutely essential that the FCA ensures that the regulation of consumer credit going forward is <u>proportionate</u> to reduce the risk of market exit.

  We believe that a FSMA-style regime for consumer credit favours large institutions such as banks and building societies and is not designed for SME's that comprise a very significant part of the consumer credit market.

  The new regime must balance any overriding desire to improve regulation, with the absolute need to create a proportionate regulatory regime. This is so that the UK can continue to have a competitive consumer credit market which not only takes account of SME's but gives them the opportunity to thrive. This will also encourage product innovation.

  There is a very real feeling that the proposals only pay lip service to the concept of a proportionate consumer credit regime.

  Proportionality is key in terms of the following:

    - Design of the new regime;
    - Costs.

- **Scale of change** – Our members are licensed by the OFT for any consumer credit activities which they engage in and they comply with the requirements of the Consumer Credit Act (CCA).

  Therefore, the vast majority of our members have had little, if any exposure in the past to the FSMA-style regime and the rules based approach. Therefore the proposals, should they go ahead, will mean that our members will have to completely change the culture of their business and the way in which they operate. The sheer magnitude of the change could in itself prompt some market exit even prior to the actual transfer date.

- **Market Exit** – Based on the proposed changes, SME's in particular are likely to leave the market - the very sector of the economy that could produce growth in the future.

  The result of SME's exiting the market is less competition. This will have a detrimental impact on consumers in terms of the charges they pay (which could actually increase) and their ability to access credit.

- **Impact on local economies** - There is a real risk that the proposed changes to the regulation of consumer credit could further exacerbate the problem on Britain's high street if bricks and mortar lenders decide to exit the market. In certain parts of the UK this could have a very serious impact on local economies.

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