



Department  
for Business  
Innovation & Skills

**CONSUMER RIGHTS BILL: SUPPLY  
OF GOODS**

**IMPACT ASSESSMENT: FINAL**

JUNE 2013

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<b>Title:</b> Consumer Bill of Rights: Supply of Goods  <b>IA No:</b> BIS0391  <b>Lead department or agency:</b> Department for Business, Innovation and Skills  <b>Other departments or agencies:</b>	<b>Impact Assessment (IA)</b>			
	<b>Date:</b> 16/04/2013			
	<b>Stage:</b> Final			
	<b>Source of intervention:</b> Domestic			
	<b>Type of measure:</b> Primary legislation			
<b>Contact for enquiries:</b> consumerbill@bis.gsi.gov.uk				
<b>Summary: Intervention and Options</b>				
<b>RPC Opinion: GREEN</b>				

Cost of Preferred (or more likely) Option			
Total Net Present Value	Business Net Present Value	Net cost to business per year (EANCB on 2009 prices)	In scope of One-In, Measure qualifies as One-Out?
£238.34m	£-23.95m	£2.78m	Yes   IN

**What is the problem under consideration? Why is government intervention necessary?**  
 UK consumer law governing the supply of goods is unnecessarily complex, there are overlaps between EU and pre-existing UK legislation, and in places the law is unclear. For example it is not clear at what point the consumer loses the right to reject faulty goods and get a full refund, nor how many repairs or replacement of faulty goods they must accept before they can pursue other remedies. This uncertainty results in business time costs and can create costs arising from unnecessary and prolonged disputes with consumers, additional staff training and the need to seek legal advice. Changes to the legal framework are required to bring clarity and certainty to both consumers and business.

**What are the policy objectives and the intended effects?**

1. To set a time period in which consumers can reject substandard goods and receive a refund.
2. To provide clarity on the number of times when retailers can repair or replace substandard goods, before being obliged to offer some money back.
3. To provide clarity on the extent to which retailers may reduce the level of refund provided (where goods are not rejected initially) to account for the use of the goods the consumer has had up to that point.
4. To consolidate and align currently inconsistent remedies available for goods supplied under different contract types.
5. To set out more clearly the standards that the goods must meet.

**What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)**

1. A 30 day period for consumers to reject substandard goods and get a refund. An exemption was considered, to allow a longer period where there is a delay before inspection may take place but this was rejected as it would undermine certainty.
2. That consumers must only accept a single attempt to repair or replace faulty goods before being entitled to some money back. An alternative of 2 repairs/1 replacement and options based on time and value were considered but 1 repair/1 replacement offers greater simplicity without unduly burdening business.
3. Consumers will receive a full refund for the first 6 months unless there is robust third party evidence for the value of the goods in which case the sum to be refunded may be reduced up to that value. A number of prescriptive approaches to calculating the refund were considered but deemed to be confusing.
4. Align remedies for different contract types
5. State consumers rights and remedies in a clearer way than at present on the face of the legislation.

<b>Will the policy be reviewed? It will be reviewed. If applicable, set review date:</b> 01/2019					
Does implementation go beyond minimum EU requirements?				Yes	
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.		<b>Micro Yes</b>	<b>&lt; 20 Yes</b>	<b>Small Yes</b>	<b>Medium Yes</b>
What is the CO <sub>2</sub> equivalent change in greenhouse gas emissions? (Million tonnes CO <sub>2</sub> equivalent)				<b>Traded:</b>	<b>Non-traded:</b>

*I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs.*

Signed by the responsible Minister: \_\_\_\_\_ **Jo Swinson** \_\_\_\_\_ Date: \_\_\_\_\_ **4 June 2013** \_\_\_\_\_

# Summary: Analysis & Evidence

# Policy Option 1

## Description:

### FULL ECONOMIC ASSESSMENT

Price Base Year 2013	PV Base Year 2013	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: 148.97	High: 352.39	Best Estimate: 250.99

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	4.6	9.5	86.0
High	11.6	12.1	115.6
Best Estimate	8.1	10.8	100.8

#### Description and scale of key monetised costs by 'main affected groups'

Business: Transition costs: Familiarisation costs £2.4m; Initial increase legal costs £5.7m.  
 Ongoing costs to business: Increase in cost of limiting mandatory Tier 1 remedies to 1 repair or replacement £2.17m; Cost of amending deduction for use £0.96m; Increase in the number of complaints to business at £0.46m; Increase costs of redress £5.7m  
 Consumers: Net cost to consumers of amending the right-to-reject period to 30 days £1.47m

#### Other key non-monetised costs by 'main affected groups'

Consumers: there may be some costs to consumers where the long-term right to reject is removed for contract types other than straight sales. This has not been quantified or monetised.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	0.0	28.6	245.6
High	0.0	50.3	432.1
Best Estimate	0.0	39.5	339.1

#### Description and scale of key monetised benefits by 'main affected groups'

Business: Ongoing benefits: Simpler complaint handling £1.48m; Reduced legal advice costs £2.45m; Reduced number of court cases £1.2m; Reduced training costs £0.79m; Net saving to business of amending the right-to-reject period to 30 days £1.47m.  
 Consumers: Ongoing benefits: Reduced risk of consumer detriment increasing from £8.32m in the first year to £9.1m by the tenth year. Reduced transaction costs increasing from £22.30m in the first year to £24.39m in the tenth year.

#### Other key non-monetised benefits by 'main affected groups'

Not applicable.

#### Key assumptions/sensitivities/risks

Discount rate (%) 3.5

We identified two key risks associated with providing a clearer legal framework for the supply of goods. Firstly, the risk that the revised framework shifts burdens onto business from consumers, or conversely undermines consumer protection. Secondly a risk that a more certain legal framework removes flexibility in the current law which is relevant to the supply of goods and could therefore disproportionately impact on some traders.

In developing these proposals we have sought to mitigate these risks by consulting widely with businesses and consumer groups to identify potential impacts (the Law Commissions consulted in 2008 and BIS consulted in summer 2012), holding workshops with stakeholders on emerging options (September 2012) and informally discussing options with a wide range of goods suppliers and consumer groups. We also commissioned the two stage IFF survey of retailers which informed our evidence of current provision of redress by traders.

### BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:	In scope of OIOO?	Measure qualifies as
Costs: 10.2      Benefits: 7.5      Net: -2.8	Yes	IN

## Evidence Base (for summary sheets)

### Problem under consideration

1. This Impact Assessment relates to proposals to reform consumer law on supply of goods. The proposals form part of a wider programme of work to reform consumer law (the 'Consumer Law Reform Programme'). This section outlines the overall motivation for clarification and consolidation of consumer law, before explaining the specific proposals covered by this IA.

### Background context:

2. The scale of the domestic trade for good is enormous, in 2011 consumers spent £401,245m<sup>1</sup> on goods and there are an estimated 356,160<sup>2</sup> goods retail businesses in the UK.
3. UK consumer law is unnecessarily complex. A bench-marking study by the University of East Anglia in 2008, found that the current system of consumer law offers a high degree of protection but is confusing, because it has grown piecemeal over the years<sup>3</sup>. Consumer law is fragmented and in places unclear, for example where the law has not kept up with technological change or lacks precision. There are also overlaps and inconsistencies between EU<sup>4</sup> and pre-existing UK legislation and the law is couched in legalistic language.
4. It is widely understood that consumers who understand their rights can play a strong part in driving growth because they force businesses to innovate and pursue efficiency<sup>5</sup>. For this they need both competitive markets and a strong but simple framework of consumer law that can be effectively enforced.
5. For traders, poorly understood law wastes business time and can create costs arising from unnecessary and prolonged disputes with consumers, additional staff training and the need to seek legal advice. Unscrupulous traders can exploit the law's complexity and undermine competition from legitimate businesses. Consumers who lack confidence in their rights are less likely to try new market entrants and innovative products, which in turn weakens competitive pressure on incumbent firms.
6. The proposals within this Impact Assessment form part of a proposed wider reform of Consumer Law (the "Consumer Law Reform Programme"). They are intended to come into effect alongside or shortly after another part of the package – regulations which will implement the Consumer Rights Directive ("CRD") – in order to clarify and update the legislative framework across the piece. The reform will require primary legislation (the proposed Consumer Bill of Rights), amendment of the Consumer Protection from Unfair

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<sup>1</sup> Consumer Trends Q3 2012, ONS: <http://www.ons.gov.uk/ons/rel/consumer-trends/consumer-trends/q3-2012/rft-web-excels---cvm-sa--q3-2012.xls>

<sup>2</sup> See para 67 for more detail on how this estimate is derived.

<sup>3</sup> University of East Anglia 'Benchmarking the performance of the UK framework supporting consumer empowerment through comparison against relevant international comparator countries' for BERR 2008

<sup>4</sup> Directive 1999/44/EC was transposed into UK law with effect from 2003, as discussed further below.

<sup>5</sup> ICF GHK 'Consumer Rights and Economic Growth' for the Department for Business Innovation and Skills (to be published 2013).

Trading Regulations as well as the implementation of the new Consumer Rights Directive through regulations. The package of reform intends to:

- **Consolidate** the law to reduce fragmentation;
- **Clarify** the law to reduce the scope for costly disputes;
- **Update** the framework to ensure that consumer rights keep pace with technological advances;
- **Deregulate** to introduce key business-friendly provisions; and
- **Enhance** consumer rights where it is appropriate to do so.

The proposals on goods are primarily intended to provide clarity and consolidate the existing law. In doing so, in some respects, the proposals deregulate for business or enhance consumer rights; these areas are explored further below.

### **Problems with the law covering the supply of goods**

7. Currently, the law on consumer rights for faulty goods is unclear and unnecessarily complicated in some instances. The Davidson Review (2006), which examined how EU Directives have been implemented in the UK as part of the then Government's regulatory reform agenda, highlighted consumer sales law as an area where the implementation had caused additional complexity, by overlaying EU law on top of the existing domestic regime<sup>6</sup>. A key finding was that, 'Following the implementation of the Consumer Sales and Guarantee Directive, the remedies available to consumers when they have been sold faulty goods are too complicated. It is unclear how best to choose between the various remedies available'. As a result, the review concluded that the law on consumer remedies was too complex, causing unnecessary burdens on business.
8. On the recommendation of the Davidson Review, BIS (as the former Department for Business, Enterprise & Regulatory Reform) asked the Law Commission and Scottish Law Commission to produce a joint report on the reform and simplification of remedies available to consumers relating to the sale or supply of goods. This report followed a consultation, which was published in November 2008<sup>7</sup>. Our proposals for a 30 day right to reject faulty goods, the application of this to all contract types for the supply of goods, and a limit of a single failed repair or replacement of faulty goods before being entitled to pursue further remedies, are based on recommendations of the Law Commissions.
9. The result of the complexity is that the law is burdensome for business to follow and consumers are often poorly informed about their rights. In some cases, consumers do not pursue remedies as they are not aware that a remedy is available to them; whereas, in other instances, consumers overestimate their rights. This in turn, can lead to costly disputes between consumers and retailers – exacerbated by the fact that in some key areas, the law is unclear as well as complex.
10. For example, the short-term right to reject faulty goods which have been purchased is a key form of redress for consumers. However, the right is currently lost after the lapse of a 'reasonable time', which must allow a buyer reasonable opportunity to examine the goods. This is a common source of dispute, as what is reasonable to one party, is often not reasonable to the other. It is difficult to determine a general 'rule of thumb' with which to

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<sup>6</sup> Lord Davison 'Davidson Review: Implementation of EU Legislation' for BRE 2006 40, Chapter 3, Para 3.20

<sup>7</sup> Available at [http://lawcommission.justice.gov.uk/docs/lc317\\_Consumer\\_Remedies\\_Faulty\\_Goods.pdf](http://lawcommission.justice.gov.uk/docs/lc317_Consumer_Remedies_Faulty_Goods.pdf)

advise consumers, as courts have come to very different conclusions depending on the facts of the individual cases under consideration.

11. Business groups, including the British Retail Consortium, consider that this results in many traders erring on the side of caution and allowing a much longer period than would be necessary, beyond one or two months in some cases, thereby increasing any potential costs caused by the depreciation in value of the goods. There is a feeling among retailers (relayed to BIS by retail trade bodies during consultation) that the courts tend to be pro-consumer and favour a longer period when judging what is 'reasonable'. Whether or not this is the case, many traders provide refunds for significant periods, taking a view as to what a court may rule.
12. Prompting reform of this area, the Government's Red Tape Challenge on Retail concluded in July 2011, that there would be significant gains to be made by rationalising and clarifying consumer law<sup>8</sup>.
13. The complexity of consumer rights in the supply of goods causes unnecessary detriment to consumers and costs to business, as outlined above. Furthermore, an ineffective scheme of consumer rights stifles competition between firms to produce the best quality products, for the best price, to consumers. This area of law requires legislative reform to make it simpler, clearer and more effective.
14. The proposals set out in this Impact Assessment are for reform of existing UK legislation, some of which derives from the EU Consumer Sales and Guarantee Directive (1999/44/EC, implemented in UK law by UK SI 2002/3045) which was a minimum harmonisation Directive. In some respects, the proposals would alter the way the provisions of this Directive have effect in UK legislation. These areas are explored below and are included in the direct costs to business set out in this Impact Assessment.

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<sup>8</sup> See <http://news.bis.gov.uk/content/detail.aspx?NewsAreaId=2&ReleaseID=420597&SubjectId=2>

## Economic Rationale for Intervention

15. The key motivation for simplifying and reforming consumer law is to make markets work more effectively and to drive economic growth.
16. Well-functioning competitive markets encourage growth by creating incentives for firms to become more efficient and innovative<sup>9</sup>. Markets can only be fully competitive if consumers are active and confident, meaning that they are willing to challenge firms to provide a better deal, switch between suppliers, and take up new products<sup>10</sup>. Consumer law reform can play a central role in empowering consumers and hence supporting more effective competition.
17. First, by simplifying and clarifying consumer law, the reforms aim to raise consumers' awareness and understanding of their existing rights. The proposed consumer law reforms will reduce and streamline the number of pieces of consumer legislation. They will also provide clarity where the law is currently not specific – for example, specifying the number of days within which consumers have a right to reject faulty goods, rather than the current provision that consumers lose the right to return faulty goods after a 'reasonable time.'
18. Greater awareness of consumer rights should make markets work more effectively because consumers will have greater confidence to switch to alternative suppliers or take up new products. Where consumers are unclear what will happen if things go wrong with a new product or service, they will take account of this risk either by engaging in costly search to find out more about the product, or by requiring a 'risk premium' on the new product. Clarifying consumer rights can thus reduce transaction costs of switching suppliers or taking up a new product. It can also help to overcome behavioural inertia, where customers prefer to stick with what they know rather than the slightly less certain (but potentially better) alternative.
19. This is particularly important in allowing new entrants to compete and win customers from established firms. For example, in online markets the strength of established brands comes in part from a perceived lack of consumer confidence in the protections afforded by consumer law for consumers purchasing from smaller suppliers.
20. Second, and related to these simplification benefits, consumer law reform can also ensure that substantive consumer protections are focused on addressing key market failures – particularly information asymmetries between consumers and firms.
21. There is strong academic support for the position that some minimum degree of consumer protection is required in order for markets to function effectively<sup>11</sup>. For example, in the absence of consumer law, consumers would typically not know how a firm would respond if something went wrong with a product or service. Having to find out this information in each case, and potentially negotiate an insurance agreement with each firm, would be extremely costly. Having a minimum level of consumer protection in place is an efficient way of reducing search and transaction costs.

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<sup>9</sup> For references to literature on the links between competition and growth, see OFT 'Competition and growth' 2011

<sup>10</sup> Mark Armstrong 'Interactions between competition and consumer policy' 2008

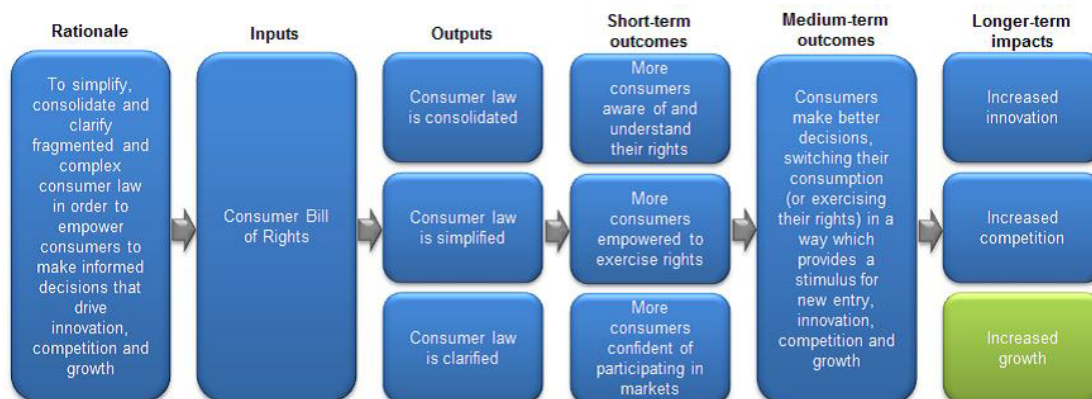
<sup>11</sup> *ibid*



22. The overall impact on growth of consumer law simplification could be significant. For example, in Australia the Productivity Commission estimated that simplifying national consumer law could increase productivity by 0.13 per cent, and in turn lead to higher GDP<sup>12</sup>. In the longer term, these productivity gains were estimated at A\$6 billion over forty years.

23. Figure 1 summarises the way simplified consumer rights can have an impact on economic growth.

**Figure 1: Logic model linking simplified consumer rights and economic growth<sup>13</sup>**



<sup>12</sup> ICF GHK 'Consumer Rights and Economic Growth' (to be published 2013).

<sup>13</sup> Model taken from ICF GHK 'Consumer Rights and Economic Growth' (to be published 2013) pg18

## Policy objectives

24. This Impact Assessment is concerned with proposals addressing consumer rights when contracting for the supply of goods. These proposals sit within a wider package of reforms to consumer law, as mentioned above.
25. We have five objectives in consolidating and providing clarity to the law on the supply of goods specifically:
- To set a clear time period in which consumers can reject substandard goods and receive a full refund, providing clarity to both the consumer and business.
  - Where the right to reject is lost or where the consumer does not choose to reject faulty goods, to provide clarity on the number of times that retailers can repair or replace substandard goods, before being obliged to offer some money back.
  - To provide clarity on the extent to which retailers may reduce the level of refund provided (where goods are not rejected initially) to account for the use of the goods the consumer has had up to that point.
  - To consolidate and align the currently inconsistent remedies available for goods supplied under different contract types, such as sale, work and materials, conditional sale or hire purchase.
  - To set out more clearly the standards that the goods must meet.
26. Clarifying and consolidating the law in this area should:
- Benefit the market as a whole by increasing consumer confidence, empowering consumers and driving stronger competition between firms.
  - Make it easier for consumers to secure redress when their rights in relation to the supply of goods are breached.
  - Reduce business costs, by allowing traders to resolve disputes more quickly and easily, and reduce expense in staff training over consumer rights.
27. Increasing consumer confidence will empower consumers to challenge incumbent firms, switch between competitors, and take up new products. In turn, this should force businesses to compete on price and quality, stimulating innovation and growth – along with greater investment in the long term.
28. Actions such as issuing guidance and providing education on the current law would be insufficient to achieve these policy objectives.
- For example, whilst it did have some success, the OFT's 2009 'Know Your Consumer Rights Campaign' was only able to address a limited amount of the confusion experienced. The 'Consumer Detriment 2012 Survey' by Consumer Focus shows that consumers continue to suffer unacceptable levels of detriment, and responses to the BIS consultation strongly suggest that a high level of confusion continues to exist.
  - Whilst it is vital that consumers are educated about their rights, the success of such education may be dependent on the clarity of its content. In a report for BIS on how consumer contract law could be simplified, streamlined and rationalised, Professor Howells and Professor Twigg-Flesner noted that where the content of the law is clear

and accessible this makes it easier to provide effective consumer education<sup>14</sup>. If consumers and businesses cannot understand the education they are given because the content is too complex, they are likely to become more, rather than less, confused.

- Behavioural economics further suggests that consumers are unlikely to be able to understand complex law. The way information is presented to them, and the ease with which it can be understood, is likely to be crucial in consumers' awareness<sup>15</sup>.

29. Therefore, the consolidation, clarification and, where appropriate, enhancement of the law is needed. This should be delivered along with consumer and business education campaigns, in order to ensure that all involved in the goods market are aware of the rights and obligations that affect them.

BIS is already working with a variety of consumer and business organisations to ensure effective education campaigns are provided alongside the changes to the law outlined below.

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<sup>14</sup> Department for Business, Innovation and Skills, 'Consolidation and Simplification of UK Consumer law' 2010. Para 4.42 (Edited by Professor Howells and Professor Twigg-Flesner)

<sup>15</sup> For example see discussion at <http://web.iese.edu/jestrada/PDF/Research/Others/L&BE.pdf> (J. Estrada 2001)

## Description of options considered

30. For a fuller explanation of the options see Annex A.

### 0. **Do Nothing** –

#### *Why rejected*

31. Not reforming the law in this area would leave consumers and businesses uncertain of their rights and obligations in the sale of goods.

### A. **Right To Reject**

#### Preferred Option

32. A fixed period of 30 days in which a consumer may reject goods which do not conform with statutory standards, except where the goods are perishable and would not reasonably be expected to last 30 days (when a shorter period may apply).

#### *Why Preferred*

33. It is important to maintain a right to reject to ensure consumer confidence to take up new products and suppliers<sup>16</sup>. 94% of consumers surveyed for the Law Commissions thought that the right to reject was important even though other remedies (such as repair and replacement) are available, particularly if the product is not fit for purpose, if the product is dangerous or because they do not want to wait for a repair or replacement. Businesses in their consultation responses and engagement with the Department have indicated their support for this clarification.

34. We considered that a fixed time period gave the most certainty over the length of a right to reject, for consumers and businesses alike. A period of 30 days was recommended by the Law Commissions<sup>17</sup> as giving sufficient time for a consumer to inspect goods<sup>18</sup>, as well as meeting the average expectation of consumers over this right<sup>19</sup>. Furthermore, the overwhelming majority of business respondents to our consultations agreed with a 28 or 30 day limit on the right-to-reject. We preferred an exception where goods are perishable and would not reasonably be expected to retain their quality up to 30 days, on the basis that consumers should return goods in a state where the presence of the fault can still be detected<sup>20</sup>.

#### Rejected Options

35. The Law Commissions proposed a further exception to the fixed period of 30 days in which a consumer may reject goods, where it was reasonably foreseeable to both the business

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<sup>16</sup> Explored in The Law Commission & The Scottish Law Commission (Law Com No. 317) (Scot Law Com 216) 'Consumer Remedies for Faulty Goods'. In a 2009 survey of 1021 consumers (undertaken for the Law Commission) 37% said the right to reject made them more confident about buying an unfamiliar brand.

<sup>17</sup> Ibid pg34. The Law Commissions consulted on a 'normal' period of 30 days for the right to reject and the majority of respondents agreed with this proposal for 30 days. The Law Commissions recommended that the law should do more to clarify how long the right to reject lasts. They recommended a 'normal' (rather than a fixed) period of 30 days in which the right to reject should be exercised, with some circumstances in which this could be extended or reduced.

<sup>18</sup> Ibid pg31 Para 3.51

<sup>19</sup> Ibid para 3.52 and Law Commission Consultation 188 Annex A, p150-152.

<sup>20</sup> This was recommended by the Law Commissions. Ibid pg31, Para 3.69

and the consumer that a longer period would be needed to inspect the goods. For example, in relation to 'seasonal goods' bought out of season<sup>21</sup>.

### *Why Rejected*

36. Consultation responses were mixed in whether they agreed with this exception and highly varied in how they envisioned that it might be implemented. We were concerned that this would detract from the intended clarity to this area of law. While there would be obvious cases of a consumer being unable to inspect goods functionally within 30 days (e.g. buying skis in May), there could be cases open to disagreement (such as buying a toy in September intended as a Christmas present), which introduce greater complexity to the law. The option would have added additional costs for business due to having to potentially provide more full refunds. While we have excluded this provision, a consumer will still have redress after 30 days in the form of Tier 1 and, potentially, Tier 2 remedies – described below and in more detail in Annex A.

## **B. Tier 1 Remedies – repairs and replacements**

### Preferred Option

37. Limiting the number of repairs or replacements (Tier 1 Remedies) to a *single repair or replacement* before consumers can insist on a 'Tier 2' remedy of either keeping the goods and receiving a price reduction, or rejecting the goods and getting a refund subject to a deduction to reflect the consumer's use (Tier 2 Remedies). In effect the retailer will be able to offer a single repair or replacement. If this repair/replacement is not provided within a reasonable time and without significant inconvenience to the consumer, the consumer can access Tier 2 remedies (this is currently the case and is required by the Directive). In addition, if a repair or replacement is provided but does not bring the goods to the standard required – either because the initial fault is still present following the repair or replacement or a further fault appears in due course – Tier 2 remedies are available; the scope for dispute will be reduced as a clear test will have been met. As such this proposal goes beyond the minimum requirement of the Directive (and its current transposition), in order to provide clarity for consumers and businesses as to the extent of their respective rights and obligations - the Law Commissions' consultation and our consultation both found these give rise to uncertainty currently. The Law Commissions' consultation also identified a particular concern of consumers that they could be locked into a cycle of failed repairs under the current provision.

### *Why Preferred*

38. The intention behind the reform of this area is to provide a clear cut-off point, beyond which consumers can insist on a Tier 2 remedy. Following consultation on various options, including limiting the time businesses could take to repair or replace goods, we recommend that a fixed limit of one repair or replacement will offer the greatest simplicity to consumers and businesses. The Law Commissions suggested a limit of a single repair or replacement on the basis that it would introduce much-needed clarity for consumers and traders and that an equal number of either repairs or replacements would be easiest to understand<sup>22</sup>.

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<sup>21</sup> See the Law Commission Report p36 Para 3.83.

<sup>22</sup> Ibid, pg61 Para 6.21 and above (the recommendation was made in relation to an expected new European Directive).

## Rejected Options

39. We also considered:

- a. Where a business failed to remedy the fault in a good after two *repairs or a single replacement*, consumers would have an automatic right to a price reduction or a rejection and refund with a deduction to reflect the consumer's use.
- b. Providing a fixed time limit in which a business could make repair or replacements (with no limit on the numbers of repairs or replacements which could be made in that time).
- c. A dis-application of the limit on repairs for any repairs which are minor in relation to the value of the product.
- d. An additional right for the consumer to access a tier 2 remedy directly if goods proved to be dangerous.

### *Why Not Preferred*

40. Consultation respondents were approximately equal in favouring the option of a single repair/replacement and the option of two repairs or a single replacement. More businesses specifically opposed a single repair/replacement scheme, but consumer groups and enforcers were generally in favour.

41. Survey evidence commissioned by BIS<sup>23</sup> suggested that providing a replacement was the most common response to a faulty good for 66% businesses<sup>24</sup>. The second most common response was full refund at 25%. Only 7% businesses said repair was their most common response to a faulty good.

42. The IFF stage 1 survey responses found that repairs were generally successful in solving problems<sup>25</sup>. Of the 31% of businesses that ever offer repairs to faulty goods, over two-thirds (68%) reported that, of the repairs carried out in the previous year, none had failed. A weighted average of the responses shows that only 6.2% of repairs fail to solve the problem<sup>26</sup>. Therefore, a single repair will resolve the majority of problems.

43. Where a repair does fail, the faults inherent in the goods are by definition more intractable and it would appear unfair to force the consumer to accept another repair (which might also fail) in such circumstances, rather than enabling them to access the Tier 2 remedies (money back or a full or partial refund).

44. As a result, it was decided that on balance one repair or a single replacement would be fair to consumers without unduly burdening business and equalising the number of mandatory repairs or replacements would have the benefit of simplicity.

45. A set time period was felt to introduce unnecessary complexity, including difficult record-keeping requirements, compared to a fixed number of repair/replacement performances.

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<sup>23</sup> Survey carried out for BIS by IFF Research, 2012-2013 (to be published 2013). 410 goods retailers were questioned about their current practices in complying with consumer law.

<sup>24</sup> IFF Survey, E2, Table 2

<sup>25</sup> IFF Research, 2012-2013 (to be published 2013). 410 goods retailers were questioned about their current practices in complying with consumer law.

<sup>26</sup> IFF Survey E19Ran, Table 20/1.

Similarly, the option where more repairs would be allowed if each was of low value in proportion to that of the produce was rejected because it would be overly complex and record keeping would be difficult.

46. The option regarding dangerous goods was rejected following arguments raised by some consultees, that in many cases a cheap and simple fix will correct the problem.

### **C. Deduction for Use when issuing refunds under Tier 2 remedy of rescission**

#### **Preferred Option**

47. As explained above, we propose that following one failed repair or failed replacement of a faulty good (Tier 1), the consumer would have the choice of whether to keep the good and get a reduction in price, or reject the good and get a refund (Tier 2). Currently the refund may be reduced to take account of the use a consumer has had of the good. Our proposal is that where the business provides a refund within six months of a purchase, the business may not make a deduction for use (i.e. must refund the full price paid); except where robust independent evidence exists, setting out a second-hand market value for the full range of the goods in question, in which case the refund may be reduced provided it is at least of that value.

#### *Why Preferred*

48. Consumer groups viewed a period in which business cannot deduct for use when issuing refunds as an important counterbalance for the proposed time limit on the short-term right to reject faulty goods. Consumer groups argued that if a good fails beyond 30 days, and still remains faulty after an attempted repair or a replacement, the consumer should be entitled to a full refund because of the extent of difficulties caused to them<sup>27</sup>. The Law Commissions recommended removing the deduction for use altogether, partly for such reasons.<sup>28</sup>

49. However, allowing a full refund up to the maximum possible legal time limit (six years in England, Wales and Northern Ireland; five years in Scotland) was seen by business respondents as potentially very costly<sup>29</sup>.

50. We considered that an appropriate compromise was to offer a six month period after purchase during which the consumer would receive the full price following a failure of repair or replacement. Our preference for a 6-month period without deduction, rather than 3, is based on the arguments raised by consultees as to the importance of a period with no deduction and consultees favouring the option within the BIS consultation which included a 6-month period with no deduction. Additionally, there is a legal presumption, in relation to the 1st and 2<sup>nd</sup> tier remedies, that a fault in goods which manifests within six months from purchase was present at the time of purchase. After that point, the law requires that the consumer prove that the fault was present at purchase in order to pursue the tier 1 or 2 remedies (see para 57).

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<sup>27</sup> Response to BIS consultation - Which? Response Q17

<sup>28</sup> The Law Commission & the Scottish Law Commission (Law Com No. 317) (Scot Law Com 216) pg66 Paras 6.40-50. The Law Commissions' recommendation was also based on findings that the deduction for use was rarely used, which seems to have changed since 2009.

<sup>29</sup> Department for Business, Innovation and Skills Consultation on Clarifying Consumer Law 2012 - British Retail Consortium Response 8, Q17

51. However, consultation responses revealed that it was particularly important for businesses that sell high value products with rapidly diminishing value, such as automotive retailers, to be able to deduct for use when issuing refunds, even relatively soon after purchase<sup>30</sup>. This is because for complex products such as cars, repairs for a number of small faults in 6 months are not unheard of, although they are rare, so it would be disproportionately costly (and different from current practice – see paragraph 92) for the retailer to offer a full refund in such cases. To mitigate against undue costs to these businesses, we propose that where robust, independent evidence exists of the second hand value of the good, the business may make a deduction for use from a refund to reflect what the good is worth at that time, even within six months of purchase. That is, a business would not be obliged to refund the full purchase price, but must refund at least the independent second-hand value.
52. Our proposal would limit the use made of the derogation under the Consumer Sales and Guarantees Directive, which enables traders to make deductions for use from a tier 2 refund. In this way our proposal goes beyond the minimum requirements of the Directive (and its current transposition). The proposal is intended to ensure that the derogation continues to be used, so that UK business is not unduly burdened, since the UK is and would continue to be among the Member States to have applied the derogation (we understand that some but not all Member States adopted measures following the derogation).<sup>31</sup> The proposal seeks to provide both businesses and consumers with greater clarity as to how the derogation may be applied and to balance their respective interests, in response to concerns of both businesses and consumers in our consultation and to how deduction for use is currently used.
53. It is important to note that whether a good is substandard in law reflects reasonable quality expectations. That is to say, if a cheap product would not reasonably be expected to last long and becomes faulty after the duration it would be expected to last, the law would not be breached so the good would not attract any type of redress.

### Rejected Options

54. Providing a prescribed scheme of maximum deductions businesses could make to refunds following a failed repair/replacement wherein the deduction would increase with time from purchase; including one option of a minimum threshold price, under which consumers could always insist on a full refund. A 3-month period for a full refund was considered. The removal of the right to make a 'deduction for use' was also considered.

### *Why Not Preferred*

55. Ultimately, we rejected all of the options that included a prescribed scheme for the calculation of a deduction following feedback from respondents.
56. Although the schemes prescribing maximum deductions were popular among consultation respondents, we were persuaded by particular stakeholder arguments opposing this type of scheme. Firstly, many goods would not be expected to retain significant value during the entire six-year period through which a claim could be made. So providing minimum refunds for consumers would be unfair on and costly to businesses in some cases. Secondly, such

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<sup>30</sup> Ibid - Retail Motor Industry Federation, 8, Q17

<sup>31</sup> The deduction for use derogation has been transposed in a number of member states, including Germany, Italy and the United Kingdom - EC Consumer Law Compendium - Comparative Analysis, Edited by Prof. Dr. Hans Schulte-Nölke in co-operation with Dr. Christian Twigg-Flesner and Dr. Martin Ebers, February 2008, pages 647 and 686.



a scheme could be confusing, by giving consumers the impression they were entitled to a minimum refund after a particular period, when the good in question might be expected to be worn out anyway and there would not in fact be a legal entitlement to any redress if it went wrong. If a threshold was introduced, it might incentivise retailers to raise costs of goods above the threshold in order to avoid the exemption<sup>32</sup>. Any scheme involving percentage deductions for use against time of purchase proved very complicated to explain and undermined the policy objective of achieving a simple set of rights. Finally, discussion with stakeholders indicated that any prescribed model would be overly complex and lack the required flexibility to address the full breadth of goods types and the amount of use a consumer may in fact have made of the goods.

57. A three month period without a deduction for use was rejected because, in the interest of minimising the number of different timescales in operation within the new legislation (e.g. the 6 month burden of proof discussed in para 50), and given the consultation responses, it seems logical to set the period at 6 months rather than 3.

58. The option to remove the right to make a deduction entirely was also rejected as only a very small minority of respondents to the consultation favoured that option, and feedback from business was that such a move would cause burden on businesses.

## **D. A Single Scheme of Remedies**

### Preferred Option

59. Traders may supply goods to consumers under a variety of contract types such as sale, work and materials, conditional sale or hire purchase. An explanation of the different contract types and the remedies that currently apply to them can be found in Annex A. Currently, there is a lack of consistency around the forms of redress available to consumers if their goods are faulty, depending on the type of contract involved. Our proposal is to apply the same scheme of redress for all types of contracts where a business supplies a good to a consumer. The 30-day short-term right to reject would apply to all transaction types (although for hire contracts, because the consumer pays for use of the goods without any transfer of ownership, there would not be a refund of the fees for past hire) – this was recommended by the Law Commissions<sup>33</sup>. The Tier 2 remedies would also apply to all contract types.

### *Why Preferred*

60. This was preferred to doing nothing. It will eliminate differences in consumer remedies between transaction types and therefore facilitate better consumer and business awareness of their rights and obligations in each situation. With a small minority of exceptions, this was considered by consultation respondents to contribute to consumer confidence by providing a clearer, consolidated and more accessible framework of remedies for faulty goods. It was also included in the recommendations by the Law Commissions<sup>34</sup>.

## **E. Expressing Rights More Clearly**

### Preferred Option

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<sup>32</sup> Majority of business consultation respondents argued this point.

<sup>33</sup> The Law Commission & the Scottish Law Commission (Law Com No. 317) (Scot Law Com 216) p55 para 5.29-5.33. However the Law Commissions' recommendation differed in that they envisaged a 30 day 'normal' period for the right to reject which could be extended in some circumstances (see para 33 above).

61. Moving from a legalistic description of what consumers are entitled to (under 'conditions' and 'warranties' implied into their contract with a business), to a clearer description of the consumer rights within the legislation (see Annex A). The rights themselves will be unchanged.

*Why preferred*

62. This re-statement of rights does not at all change the underlying law and protections available to consumers. However, it is intended to improve consumer and business awareness of their rights and obligations. Virtually all consultation respondents agreed in principle.

## Preferred Option

63. The combination of preferred policy options provides what we consider as the best balance between consumer and business interests, while ensuring better clarity and its associated benefits for both parties.

**Table 1: Overview of preferred policy options and impacts**

Title	Starting position	Regulatory Change (+)
<b>Right to Reject</b>	Consumer can reject faulty goods that they have bought within a 'reasonable time'. It is unclear what is 'reasonable' in practice, as it depends on the circumstances of each case.	Introducing a fixed period of 30 days (less for perishable goods) in which a consumer may reject a faulty good.
<b>Tier 1 Remedies – repairs and replacements</b>	<p>Consumer may compel a repair or replacement for a faulty good. Further redress (Tier 2) is available if the repair or replacement is not done without 'significant inconvenience' for the consumer or within a 'reasonable time'.</p> <p>Unclear what amounts to 'significant inconvenience' or 'reasonable time' in practice. Currently businesses could potentially carry out more than 1 repair or replacement before having to offer this further redress.</p>	Imposing a limit of 1 repair or 1 replacement before the consumer can insist on further redress (Tier 2).
<b>Deduction for use when issuing Tier 2 refunds</b>	<p>Consumers may, after failed repair(s)/replacement(s) (i.e. under the above criteria), insist the business offers either reduction in price (if the consumer keeps the goods) or refund (if the consumer gives back the goods). If a refund is required, the business may make a deduction for the consumer's use of the good.</p> <p>There is no statutory limit on the deduction that can be made.</p>	Creating a six month period within which business cannot deduct from the refund, where they may currently; although there will be an exception where the business can supply evidence of independent third-party reference pricing for goods in question. After the initial six months of the contract, the general rule will remain as currently (but where there is such reference pricing then a refund still must be of at least that value).
<b>A Single Scheme of Remedies</b>	<p>Various types of supply of goods contracts exist and at present a variety of remedies relate to each, with little logical reason for the differences.</p> <p>For example, a normal 'sale' contract attracts a short-term right to reject and Tier 1 and 2 remedies. Consumers buying goods and services together (e.g. goods to be installed), or goods under conditional sales or hire or hire-purchase have a long-term right to reject. Consumers hiring goods or buying on hire-purchase have no Tier 1 or 2 remedies.</p>	<p>Changing consumer entitlements across contract types to normalise remedies.</p> <p>The long-term right to reject will be replaced with a short-term right to reject so that the 30 day right to reject will apply to the supply of goods under all contract types (albeit the refund payable will differ for hire – see Annex A).</p> <p>Tier 1 and Tier 2 remedies will be introduced for hire and hire-purchase so that they apply to all contracts for the supply of goods.</p>
<b>Expressing Rights More Clearly</b>	<p>Consumers have rights described as 'conditions' and 'warranties' which are 'implied' into the contract for the goods they are buying. This means that the goods must meet quality standards</p> <p>This is too legalistic for most consumers.</p>	<p>Taking the same rights which exist but stating them more clearly on the face of the law.</p> <p>No change to the consumer rights themselves.</p>

64. Please see Annex A for further detail and Annex B for diagrams of the relationship between the remedies for goods in the current law and in our proposals.

## Estimating the number of businesses within scope of the reform

65. The majority of businesses that sell goods to consumers will be within scope of the changes covered by this Impact Assessment. As businesses can provide both goods and services to consumers, trying to estimate the number of businesses within scope of the changes to the supply of goods is difficult. Previously, the scope of businesses selling either goods or services to consumers has been defined as all retail, accommodation, automotive and personal service enterprises.<sup>35</sup> Using this definition and the 2012 Business Population Estimates for the UK, this was estimated to be 742,000 businesses.<sup>36</sup>
66. Many of these businesses will be providing only goods or services to consumers. Therefore a figure of 742,000 is likely to be an over-estimate of businesses affected by the reforms to supply of goods consumer law.
67. To account for this we have used the proportion of household expenditure on goods and services (48% goods, 52% services)<sup>37</sup> to estimate the number of businesses providing goods, yielding an estimate of 356,160 (48% of 742,000). Of this population, 93% are micro employers with less than 9 employees<sup>38</sup>.

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<sup>35</sup> Department for Business, Enterprise and Regulatory Reform: 'Impact Assessment: The Consumer Protection from Unfair Trading Regulations' 2008

<sup>36</sup> <https://www.gov.uk/government/organisations/departments-for-business-innovation-skills/series/business-population-estimates>

<sup>37</sup> Office for National Statistics: Consumer Trends, Household final consumption expenditure, Total Expenditure, table 0GSKS

<sup>38</sup> The IFF survey used a different methodology for estimating the affected business population. They used the Business Population Estimates and assigned different types of businesses to be either service or goods providers.

## Monetised and non-monetised costs and benefits of each option

68. Reforms to consumer law on the sale of goods are part of a suite of proposed improvements to consumer law to be introduced through the Consumer Law Reform Programme.
69. Many of the impacts are common across all the proposed changes to consumer rights law. In these cases, we have apportioned an appropriate share of the impact to the changes relating to goods, as explained in the text. The following analysis also outlines specific impacts of reform of the law in relation to faulty goods.
70. In order to get a better understanding of the potential impacts of the proposed reforms, we consulted stakeholders and commissioned an independent survey of businesses. The survey was conducted by IFF Research Ltd. (an independent research company), on behalf of the Department of Business, Innovation and Skills during the autumn of 2012. This project comprised two stages: the first stage gathered data on current business practices in relation to treatment of complaints and redress given to consumers of faulty goods. The second stage of the survey involved the return by a smaller sample of businesses of a cost sheet of estimates for expenditure and resources allocated to consumer rights issues, coupled with an interview to ensure cost sheets were filled in consistently<sup>39</sup>.
71. Table 2 summarises the established costs and benefits of the different proposed measures. More detail of the estimates is given in the following paragraphs.

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<sup>39</sup> Stage 1 of the survey was conducted on 1,000 businesses engaged in business-to-consumer trading (for goods, digital and services). Stage 2 involved a selected sample of 60 Stage 1 participants who provided additional detail on their Stage 1 responses.

**Table 2: Summary of costs and benefits of preferred options**

Type of Cost/Benefit	Impact	High (£ million)	Low (£ million)	Best Estimate (£ million)
<b>Transition costs to business</b>	Familiarisation costs	3.47	1.33	2.40
	One-off transitional legal costs	8.16	3.27	5.71
<b>Ongoing costs to business</b>	Increase in cost of limiting Tier 1 remedies to 1 repair or replacement	4.35	0.00	2.17
	Cost of amending deduction for use	0.99	0.93	0.96
	Increase in the number of complaints to business	0.73	0.18	0.46
	Increase in redress for consumers resulting from complaints	7.61	3.80	5.71
<b>Ongoing costs to consumers</b>	Net cost from amending the right-to-reject period to 30 days	2.20	0.74	1.47
<b>Total Cost (PV)</b>		115.6	86.0	100.8
<b>Ongoing benefits to business</b>	Less time spent on each complain and more junior staff able to handle a larger proportion of complaints	2.01	0.96	1.48
	Reduction in legal advice costs	3.27	1.63	2.45
	Reduction in number of cases escalating to court	1.63	0.82	1.22
	Reduction in ongoing training costs	1.22	0.37	0.79
	Net Benefit from amending the Right-to-reject period to 30 days	2.20	0.74	1.47
<b>Ongoing benefits to consumer</b>	Reduction in transaction and search costs <sup>40</sup>	29.7	14.9	22.3
	Reduction in risk of consumer detriment <sup>41</sup>	8.48	8.16	8.32
<b>Total Benefit (PV)</b>		432.1	245.6	339.1
<b>Equivalent Annual Net Cost to Business</b>				2.78

<sup>40</sup> These benefits will increase annually by 1%, in line with the forecasted increase in household expenditure.

<sup>41</sup> These benefits will increase annually by 1%, in line with the forecasted increase in household expenditure.

## **Costs to Business**

72. The costs arising from the change in legislation will be incurred by business and include:

- Familiarisation costs
- Initial increase in legal costs
- Cost of handling increased number of complaints to business
- Cost of increase in redress for consumers resulting from complaints
- Impact from reducing number of Tier 1 remedies a business is obliged to offer
- Impact from changes to deduction for use arrangements

## **Transition Costs**

### *Familiarisation Costs*

73. We anticipate that all goods retailers will incur familiarisation costs from the proposed reforms to the sale of goods law, but these costs will be relatively small because the changes are intended to simplify existing law, making it easier to understand and apply. Moreover, as the proposals on goods will be introduced in parallel with the Consumer Rights Directive and other reforms within the Consumer Bill of Rights we believe that the cost incurred may be lower than if these changes were introduced in isolation (synergy in familiarisation and training provision).

74. As the proposed reforms are predominantly intended to provide clarity in relation to the existing legal position, we do not think it will take more than 10-20 minutes for a staff member to become familiar with the changes. This is based on the assumption that the training for all consumer rights reform will be delivered in one session, of which 10-20 mins would be spent on the goods changes. This is underpinned by the plan to include an awareness campaign as part of the reforms and the reality that most businesses are informed of changes by their trade associations and businesses groups, and are likely to read purpose-drafted literature about the changes. Cumulatively, for all the changes to consumer rights addressed in the various Impact Assessments within the Consumer Bill of Rights package, training is estimated to take around two hours in total.

75. As stated above, most goods firms are micro businesses with 9 or fewer staff members. For these, we assume that consumer complaints are typically handled by a senior staff member (often the owner or proprietor). Therefore we have based our familiarisation cost on the wages costs for Customer Service Managers and Supervisors, at £15.55 per hour<sup>42</sup>. Assuming the time taken for familiarisation is 10-20 mins as noted above, the average cost per business would be £2.59 to £5.18. Extrapolated across the business population, the overall cost is in the range £0.9m to £1.85m, with a best estimate of £1.38m.

76. For larger firms with 10 or more employees, we have assumed that staff at management level would be familiarised with the reforms (included above at the same wage cost noted

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<sup>42</sup> This is based on ASHE 2012 hourly wage of £13.58 for Customer Service Managers and Supervisors, with non-wage labour costs at 14.5%, giving an hourly cost of £15.55

above for customer service managers and supervisors). We estimate that in addition, there would also be familiarisation costs in training 10-20 frontline staff members on the reforms at an hourly cost of £9.78<sup>43</sup>. This is a cost across the business population of 356,128. This will result in an overall cost for larger firms in the range £0.41m to £1.63m, with a central estimate of £1.02m

77. In total we estimate businesses will incur familiarisation costs of £1.33m to £3.47m, with a mid point best estimate of £2.4m.

### *One-off transitional legal costs*

78. We anticipate that the reforms under the Consumer Rights Bill, in parallel with the Consumer Rights Directive, may initially lead some businesses to seek additional external legal advice. This is likely to be a one-off transition cost to help business apply the reforms.<sup>44</sup> Based on the responses to the IFF survey, only a small proportion of businesses (20%) sought external legal advice in the last year<sup>45</sup>. As the reforms do not represent significant legal change such as entirely new concepts, we believe that there will only be a small increase in legal advice costs. We used the data from the IFF survey on annual legal costs<sup>46</sup> to estimate the impact of an increase of 2-5%. This was done by firm size to reflect the variation in legal advice costs faced. We have estimated a cost range of £3.27m to £8.16m, with a central estimate of £5.71m

## **Ongoing Costs**

### *Increase in the number of complaints from consumers and subsequent increase in costs to business of giving redress to consumers*

79. We expect that the clarification of rights will increase slightly the number of complaints to business in relation to Goods. There may be consumers who are currently eligible to complain and receive redress who are unaware of their rights. We expect that under the proposed legislation a proportion of these consumers will exercise their rights, resulting in increased costs for business.

80. It is difficult to estimate how many more consumers will seek redress as a result of the changes to statutory remedies, because this will depend on consumers' behavioural response to the new regime which cannot be observed from current market data. According to the Consumer Detriment 2012 survey, 25% of problems experienced by consumers had not been pursued and consumers have no intention of doing so<sup>47</sup>. For 66% of problems, consumers had complained or taken action to try to resolve the problem, of which around a half were considered resolved by the consumer.

81. To estimate the scale of the impact, we have assumed that the number of complaints to business might increase by 5-10%, (i.e. the 66% of problems where consumers took action, as cited above, would increase to around 69.3%-72.6% of problems under the new regime). Based on a baseline estimate of 704,650 complaints<sup>48</sup>, this suggests that the new policy

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<sup>43</sup> Based on ASHE 2012 hourly wage for frontline customer service occupations at £8.54, uprated to include 14.5% non-wage labour cost is £9.78 per hour.

<sup>44</sup> In the longer term we expect firms to have less need for legal advice, as set out in the benefits section below.

<sup>45</sup> IFF survey D3, Table31

<sup>46</sup> Average annual legal advice costs were £684 for micros (population 332,311), £23,654 for small, medium and large firms (pop 23,817)

<sup>47</sup> <http://www.consumerfocus.org.uk/files/2012/10/TNS-for-Consumer-Focus-Consumer-Detriments-20121.pdf> Section 7.4

<sup>48</sup> Total Number of complaints is 2,040,000 (This figure is a combination of the 2012 Consumer Detriment's cited number of problems (15.7 million) (page ii) and the Consumer Conditions 2011 percent of complaints directed to business in the UK (13%) (page 42)). The proportion of



might lead to between 35,200-70,500 additional complaints. We consider that this is a conservative estimate (i.e. errs on the side of over-estimating business costs) because there will only be a limited subset of consumers who will be influenced by changes in consumer law to complain more.

82. These additional complaints will impose costs on businesses in two ways.

- First, businesses will face the time costs of complaints handling. We have assumed first that complaints handling takes 20-40 minutes per complaint on average, based on responses to the IFF survey. Taking this as our baseline, we have estimated an increase in complaints of 5-10% leading to a cost in the range £0.18m-£0.73m, with a best estimate of £0.46m. (Note that we expect this increase in volume of complaints will be offset by reduced costs of handling each complaint, which is discussed under benefits to business).
- Second, in some cases, businesses will have to offer redress to consumers. The IFF survey suggests that, on average, 57% of Goods complaints are resolved without providing remedies (i.e. required only additional information to resolve) – so we assume that 43% of the additional complaints will lead to a requirement for redress. The weighted average cost of redress offered by business in the IFF survey is £251. Multiplying the additional number of additional unresolved complaints<sup>49</sup> by the average cost of redress suggests additional business costs in the range £3.80m-£7.61m with a best estimate of £5.71m.

83. Adding these two costs together gives a net additional cost to business of £4.98m-£8.34m per year, with a mid point best estimate of £6.17m.

#### *Tier 1 Remedies- 1 repair or 1 replacement*

84. If a consumer discovers that goods that they have bought are faulty, they have a right to have the goods repaired or replaced. These are known as the Tier 1 remedies. A consumer cannot insist on one of these if it is disproportionately costly in comparison to the other (so, for example, a consumer cannot insist on having a toy repaired when it would be far cheaper for the retailer to offer a replacement).

85. If repair and replacement are impossible, or if one is not provided within a reasonable period or without causing significant inconvenience to the consumer, the consumer has the right to access Tier 2 remedies; a reduction in price or rejection of the good with a refund (rescission). Tier 2 remedies are explored in more detail below. A business may argue that a further repair or replacement can be provided if a first repair or replacement was provided in good time and without inconveniencing the consumer, if the fault recurs or a further fault occurs.

86. Under the proposed reforms, business will be required to provide one repair or replacement of faulty goods (subject to the same restrictions as currently) and where this fails they will then be obliged to provide a Tier 2 remedy (price reduction or refunding). Thus, businesses may incur costs in providing a more expensive form of redress earlier (Tier 2), where they may currently replace or repair more than once persistently faulty goods.

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complaints to goods firms has been estimated using the number of goods, services and digital content firms in the business population estimates (37% services, 35% goods and 28% digital content).

<sup>49</sup> This is the new baseline of complaints (current with 5-10% increase) by the rate of unresolved complaints which require the provision of redress

87. The Law Commissions' research in 2009 concluded that consumer expectation is generally to only have to accept one replacement, and if that replacement proved unsatisfactory, they would expect to receive a refund. This is on the basis that consumers are likely to have lost faith in the product if the replacement also fails. The Law Commissions also noted that accepting only a single replacement is common practice among other member states. On the basis of this, the Law Commissions consulted on the limiting to a single replacement and received strong support for this proposal. Further to this, responses to the BIS consultation (which proposed the same), and feedback obtained through discussion with stakeholders, presented no express objection to a limit of a single replacement. We therefore agree with the Law Commissions' proposal on this issue.
88. However, the IFF survey demonstrated that 11% of goods retailers currently sometimes carry out more than one repair to a good, and this was consistent with information from some of our stakeholder discussions and consultation responses. We have used the IFF survey responses on businesses' average annual cost of repair and have therefore used the repair data as the basis for our costing calculations for changes to tier 1 remedies. From this we assumed that there will be costs of moving to the new regime i.e. moving sooner to Tier 2. As there is no available data on the cost of repair versus a reduction in price or refund, we have conservatively assumed that the cost would be up to double that of a repair. This is based on the assumption that the arrangement and logistics for carrying out repairs is already in place (so likely to be lower than providing a Tier 2 remedy). We have estimated the range at zero to £4.35m, with a best estimate of £2.17m.

#### *Deduction for Use*

89. Under existing EU-derived legislation, consumers have rights when Tier 1 remedies fail (pursuant to the criteria set out in paragraph 85 above); they can require a Tier 2 remedy of either a price reduction or refund. Currently businesses can deduct from the Tier 2 refund to take account of the use the consumer has had of the good. Under our proposed reforms, business will not be able to deduct for use within the first six months from delivery. This will result in some costs as a refund of a six month old faulty item will cost more if the retailer has to refund the full purchase price, rather than taking account of the consumer's use of the goods. We expect that costs to goods retailers as a broad category will, however, be minimal, from the analysis set out below. This is helped in part by excluding from the 6-month restriction retailers of goods for which there is robust independent evidence of the second hand value e.g. the motor vehicle industry – such retailers must instead refund at least that value (see paragraph 92).
90. Responses to the consultation and discussions with business groups indicate that many large retailers, including most of those represented by the BRC, for example, currently offer full refunds when Tier 2 remedies are required in the first 6 months, or even throughout the first year. Those companies will therefore be unaffected by any change.
91. For all other retailers we estimated the impact by using the IFF data to calculate the number of businesses who do not currently give refunds within 6 months, when Tier 1 fails. The IFF survey shows that 6.2% of Tier 1 remedies fail to correct the problem<sup>50</sup>. This isolates the percentage of firms who move to tier 2 remedies. We excluded the motor vehicles from this population as they would be covered by the proposed exemption for sectors for which

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<sup>50</sup> IFF Survey E19Ran, Table 20/1

independent third-party evidence of second hand values exist<sup>51</sup>. We analysed the data by business size as the evidence suggests variation in costs and approach depending on the size of the business<sup>52</sup>. To calculate the cost of obliging these businesses to pay a full refund for the first six months, we estimated their current costs from replacements<sup>53</sup> or repairs<sup>54</sup> (this provides the range as not all business currently opt for the same remedy and so will face different costs in complying) and then estimated how much the provision of full refunds would cost them. The difference between the current remedies and the proposed is the additionality of this reform. Based on this methodology, we estimated the cost to business as being in the range £0.93m to £0.99m, with a best estimate of £0.96m.

92. We separately considered whether there would be any impact on firms or consumers in excluded sectors - notably motor vehicles - where the new law would allow deduction for use but require a refund to be no less than the objective second-hand value, compared with the current system of a deduction to take account of use. We have concluded that there will be no significant impact for the following reasons
93. Under the existing law, businesses in the motor vehicles trade can offer a repair/ replacement to a customer and subsequently, where they fail (as per paragraph 85 above) to correct the fault, a Tier 2 remedy (including refund from which they can deduct for use). In practice, under the current law refunds very rarely happen because retailers will offer repairs instead, and customers tend not to want to push for a refund.
94. The proposed reforms on repair/replacements aim to reduce the risk of consumers getting trapped in a cycle of repairs to their motor vehicle (where they are not aware that they are entitled to a refund). However, under our proposals, if they wish, they could request additional repairs before moving to a Tier 2 remedy. The trader would, as now, be obliged to provide these repairs free of charge. The only exceptions are if the repair is impossible or if it is disproportionately expensive in comparison to the other tier 1 remedy, replacement. In the motor industry, it is highly unlikely that a repair would be disproportionately more costly than replacing the vehicle, so in effect, the consumer can continue to ask for repairs for as long as repairs remain possible, if that is their preference.
95. Where a refund does occur, the current law allows a deduction to be made to take account of the use the consumer has had of the goods, irrespective of whether the goods are returned within 6 months. For motor vehicles, the Society of Motor Manufacturers and Traders (SMMT) indicated to us that if a dealer currently needs to calculate a refund value, they will take into account:
- Mileage
  - Any damage
  - Wear and tear
  - Duration of ownership/use
  - Reference to Glass's Guide for second hand car values
  - Dealer's trade-in value (if the consumer wishes to purchase a different car from the same dealer)
96. Under our proposals, the law will continue to allow a deduction for use in the motor vehicle sector. The only change is to specify that this deduction must not reduce the refund below the second hand value of the goods, as determined by objective, third-party sourced reference pricing. However, as stated above, in practice motor dealers already use second-hand values as a basis for estimating the deduction for use under the current law. Therefore, we expect there to be no systematic change in the level of deduction for use as a result of the new threshold.

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<sup>51</sup> In scope populations: micros 292,851, small firms 15,769, medium firms 1,566 and large firms 372.

<sup>52</sup> Average annual cost of full refunds: micros £177, small firms £1,869, medium firms £37,320, no data was available for large firms.

<sup>53</sup> Annual cost of providing replacements: micros £58, small firms £1891, medium firms £3,600, no data was available for large firms.

<sup>54</sup> Annual cost of providing repairs: micros £100, small firms £264, no data available for medium or large firms.

97. This analysis is supported by industry participants. For example the Retail Motor Industry Federation (RMI), whose membership includes franchised car and commercial vehicle dealers, independent garages and motorcycle dealers, stated that the Option 4 (the only option which included reference to objective evidence of second-hand value) 'allows for continuation of business practice'. The RMI told us in response to the consultation that the deduction for use is a key ability for traders that must be maintained. The removal of such ability would cause significant cost increases in the purchase price of products. The RMI stated, 'Option 4 allows for the continuation of business practice, providing consistency across all motor retailers and providing a clear framework of expectation for consumers.' In respect of new vehicles, the Society of Motor Manufacturers and Traders Limited (SMMT) have told us that refunds are rare. Conciliation with the aim of agreeing on an appropriate remedy is usually done amicably direct with the dealer or with the manufacturer's customer services department, or through the conciliation/arbitration service offered by Motor Codes Ltd under the Motor Industry Code of Practice for New Cars<sup>55</sup>.

### *Single scheme of remedies for goods: eliminating long-term Right-to-Reject*

98. The main costs to business from the single scheme of remedies will come from applying Tier 1 and 2 EU-derived remedies to Hire and Hire-Purchase contracts. This means that in future, businesses could be faced with consumers insisting on repair or replacement of faulty goods under these contracts (followed by a price reduction or refund if the repair/replacement is unsuccessful), where they do not currently have to offer this type of redress. However, currently consumers can claim for damages under the long-term right to reject, and replacement is the most favoured remedy by business – with 31% of firms sometimes opting to repair faulty goods as well<sup>56</sup>. We therefore estimate that this will have a negligible impact on business.

## **Costs to Consumers**

### *Impact of clarifying the right to reject at 30 days.*

99. Amending the right to reject to 30 days will have three main impacts on consumers:

- a. It will result in costs for any consumers of goods from businesses which currently provide refunds for more/less than 30 days if goods are faulty;
- b. It will result in benefits for consumers who currently receive refunds for faulty goods within a limit of less than 30 days
- c. It will provide clarity in the law, thus reducing the current scope for debate over entitlement to a refund.

100. The first two of these effects can be treated as transfers between businesses and consumers relative to the current position under existing law. As set out at paragraph 126, we estimate that the overall impact will be a net benefit to business in the range £0.74m to £2.20m with a best estimate of £1.47m. Therefore, the net transfer cost to consumers will be equal and opposite to the business impact. Overall this results in a small net cost to consumers of £1.47m (costs net of benefits).

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<sup>55</sup> Motor Codes is a Trading Standards Institute approved Code Sponsor. Nearly all vehicle manufacturers are subscribers to the New Car Code. Citizens Advice also signposts Motor Codes for all consumers with new vehicle (and service and repair) complaints.  
[http://www.motorcodes.co.uk/images/stories/documents/code\\_document\\_web.pdf](http://www.motorcodes.co.uk/images/stories/documents/code_document_web.pdf)

<sup>56</sup> IFF Survey, E1, Table 1

101. The clarification benefits of moving to 30 days, along with wider clarifications to consumer law, are considered in the consumer benefits section below (paragraphs 129-140).

### *Costs to consumers from changes to non-normal sales*

102. Currently consumers who have purchased faulty goods as part of work and materials, conditional sale or barter/exchange contracts have the right to reject the goods and terminate the contract. This right is not lost unless the consumer knows of the fault and does something (expressly or implicitly) to show he elects to continue the contract – otherwise it continues up to the legal limitation period (6 years, except for Scotland where it is 5 years). This right therefore potentially lasts longer than the right to reject following a normal ‘sale’<sup>57</sup>, which expires after a reasonable time. Consumers with these contracts also have rights stemming from the Consumer Sales Directive, i.e. they can require the trader to repair or replace the goods (Tier 1 remedies). In some circumstances the consumer could move onto Tier 2 remedies of a reduction in price or rejection with a refund.
103. The changes we propose would affect work and materials, conditional sale and barter/exchange contracts by replacing the long term right to reject with a short term right to reject (30 days), and by simplifying the Directive-derived remedies to one repair or one replacement before the consumer could demand a Tier 2 remedy. In effect it means if a fault arises in the goods after 30 days the consumer would have to, in most circumstances, accept a repair or a replacement to the goods, but if that failed to rectify the fault or a second fault arose, the consumer could then reject the goods and get a refund (or keep them and get a price reduction) under Tier 2. In effect this means that beyond 30 days the consumer would have one extra step (repair or replacement) to get through before reaching a right to get some money back. As explained below, we think this effect would be limited in practice because we understand from consultation responses that the current rights are not widely known (see paragraph 107).
104. Currently consumers who contract for goods under hire or hire purchase have a long term right to reject (as explained above) should a fault arise. However, at common law they are not automatically entitled to recover all of the money paid under the contract, up to the point of termination.<sup>58</sup> They do not have rights under the Consumer Sales Directive so would not be able to insist on a repair or replacement (see Annex A, paragraph 14).
105. Under our proposals the long term right to reject goods under hire and hire purchase contracts would be removed and instead the consumer would have a right to reject for the first 30 days of the contract. Under hire-purchase contracts, the consumer would get a full refund. Under hire contracts, because the contract is not for ownership but only temporary use, the consumer would only be refunded any proportion of the hire fees paid which related to hire time paid for but not received. For hire and hire-purchase contracts our proposals extend the Directive-derived rights in order to achieve alignment and simplicity of the law, so the consumer could insist on one repair or one replacement, and then if that failed, could insist on a price reduction or rejection for a refund, which would be a full refund for the first 6 months in most cases.

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<sup>57</sup> Please see Annex A paragraph 13 for the different types of supply of goods.

<sup>58</sup> This was established by the 1962 case of *Yeoman Credit Ltd v Apps*. But the damages awarded in such cases have tended to be generous – e.g. equivalent to the money paid or with a small deduction for use. There is therefore some uncertainty as to how damages may be calculated in this situation and thus how much may be recovered.

*Example: a washing machine bought on HP develops a fault after 3 months' use.*

106. Now: consumer could reject the washing machine. Law is not clear on how much the consumer will be refunded (e.g. payments already made may be forfeited). Under our proposals: trader is obliged to repair or replace the washing machine. If the same or a different fault arises in the repaired washing machine or its replacement the consumer can claim a price reduction or reject the machine and get a refund. This would be a full refund for the first 6 months, a partial refund thereafter, to reflect the consumer's use of the machine. Under our proposals the consumer with a faulty washing machine has the same rights and remedies regardless of whether it was bought on HP or as a straight sale.

107. While consumers will lose the long-term right to reject goods outright in a significant number of cases, we do not believe that they will be significantly disadvantaged by the proposed changes for two reasons:

- Overwhelmingly, respondents to our consultation agreed that the proposed alignment of the goods remedies for the various different contract types under which goods can be acquired would be simpler, clearer and fairer. Those who agreed included Citizens Advice, Consumer Focus, British Retail Consortium, many other business respondents, the Office of Fair Trading, Trading Standards Institute and most local Trading Standards authorities;
- From our engagement with consumer groups we understand that the take up rate for the existing long-term right to reject is low. Citizen's Advice told us in their consultation response that 'the advantages of the long-term rights (sic) to reject are not well-known and we believe that their complexity has meant that they are seldom used'<sup>59</sup>. The Law Commissions in their report on faulty goods remedies referred to the courts having struggled with the different remedies according to contract types, and stated, 'If judges and lawyers are confused by the law in this area, it is unrealistic to expect consumers to understand it.'

108. We know that consumers seldom obtain legal advice in consumer disputes. Moreover, some consumer advisers have told us that they find it difficult to advise consumers on this area. The majority of consultees expressed the view that it is paramount that the law should be simple enough for consumers to understand and use'.

109. Citizens Advice told us in their consultation response, 'We think that this [aligning remedies across goods contract types] is a sensible change because:

- it aligns consumer rights and remedies so they are easier to use and understand;
- the advantages of long-term rights to reject are not well known and we believe that their complexity has meant that they are seldom used; and
- hire and hire-purchase will gain from clear rights to repair, replacement and refund.

110. As discussed above the changes to the long-term right to reject will simplify the law for both consumers and retailers. Due to the lack of robust data on the scale of take up for the existing long-term right which Citizens Advice believes to be low, it has not been possible to provide a definitive figure for the impacts from the proposed changes. We have estimated that non-normal sales account for approximately 2.5%<sup>60</sup> of total sales in the UK in 2011,

<sup>59</sup> Response to Department for Business, Skills and Innovation Consultation On Clarifying Consumer Law response - Citizens Advice 10, Q21

<sup>60</sup> This figure is based on data from the ONS *Family Spending 2012 Edition* and includes 'conditional sale', 'barter or exchange', 'works and materials', 'hire purchase', and 'hires'. Barter or exchange makes up a negligible portion of consumer spending. Conditional sale and hire

(based on data from the ONS *Family Spending 2012 Edition*<sup>61</sup>) and so believe that the number of consumers affected by the changes will be low, taking into account that many do not currently take up the long-term right to reject option.

## **Benefits to Business**

### **Ongoing benefits**

#### *Simpler Complaint Handling*

111. A key objective of the Goods reforms is to provide clarity for consumers and businesses on their rights and obligations in the event goods are faulty. We envisage that the proposed changes will result in quicker and easier handling of complaints for business, where less time and staff resource will be required to resolve issues; including moving complaints handling to more junior staff because procedures and remedies can be simplified and easily applied.
112. The British Retail Consortium commented in their response to our consultation, 'Clarity means that both consumers and retailers start from a common understanding of actual legal rights which should reduce the potential for disputes arising from exaggerated claims by consumers or offers below the legal minimum by retailers'.
113. To estimate the impacts on business of simpler complaint handling we took the volume of complaints (including the increase in number of complaints as in paragraph 79-83) and assumed that there would be a slight decrease in time (handling) costs of 5-10 mins. We estimate that these reforms will make it easier for businesses to handle complaints and decide quickly which complaints have merit, which require a standard response/remedy and which need to be escalated for legal advice. As with the familiarisation costs, these savings are based on Customer Service Managers and Supervisors, at £15.55 per hour<sup>62</sup> (as our research shows that currently in the majority of cases, complaints are handled by senior staff members<sup>63</sup>). Based on the business population assumptions, this suggests estimated savings of £0.96m to £2m, with a best estimate of £1.48m. We believe that some businesses may wish to reduce the number or seniority of staff handling complaints but it was not possible to quantify and monetise this additional potential benefit.

#### *Reduction in legal costs because of clarification of the law*

114. Linked to simpler complaint handling and based on simplified legal requirements, we estimate that businesses will incur reduced legal costs as a result of the reforms. According to the responses to the IFF survey, approximately 20% of businesses sought external legal advice in the previous year<sup>64</sup>. Based on the population of businesses that incur legal

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purchase represent £9,705 million per year, while hire and 'work and materials' contracts sum to £6,939 million per year. This represents 2.53% of total consumer spending in 2011 (£658,864).

<sup>61</sup> <http://www.ons.gov.uk/ons/rel/family-spending/family-spending/family-spending-2012-edition/index.html> on 15 April 2013.

<sup>62</sup> This is based on ASHE 2012 hourly wage of £13.58 for Customer Service Managers and Supervisors, with non-wage labour costs at 14.5%, giving an hourly cost of £15.55. IFF Survey F2, Table 1 shows that 83% of goods firms without dedicated customer service department have their senior managers deal with consumer complaints.

<sup>63</sup> IFF Survey F2, Table 23

<sup>64</sup> IFF Survey D3 Table 31

costs<sup>65</sup>, we have conservatively assumed a reduction of 1-2% in legal advice costs. This suggests savings of £1.63 to £3.27m, with a best estimate of £2.45m.

#### *Reduced number of cases escalating to court*

115. The clarification through the proposed reforms is also expected to reduce the number of consumer complaints which escalate into court cases. This is based on raising the understanding of both consumers and businesses on rights and obligations, and clarifying the language of the legislation.

116. The IFF survey indicated that only a small percentage of businesses (2%) had incurred costs for court cases in the previous year, and so we assume that only a small proportion of the business population will experience savings. We calculated the impacts using IFF survey evidence, splitting business into two groups (micro/small and medium/large) as the estimated costs varied significantly based on business size<sup>66</sup>. We have conservatively estimated a saving of 5-10%, due to the clarifications. As with the savings in legal advice costs, we have assumed that due to the simplified laws, complaints are less likely to end up in court because the rights and remedies will be clearly set out. We estimate that the annual savings to business will be between £0.82m and £1.63m, with a best estimate of £1.22m. This is also likely to be a conservative estimate as it is based on the cost of legal fees and not on the full cost of going to court to contest the case (e.g. time spent not on the shop floor).

#### *Reduction in ongoing training costs*

117. Although we have estimated an initial increase in training costs as businesses inform their staff about the reforms, we believe that after the initial period, training costs should decrease with business experiencing savings over time. This is primarily due to clarification of the law where businesses no longer have to interpret their obligations or prepare scenario responses and can reduce training times accordingly.

118. Based on the IFF data, only a proportion of businesses currently provide ongoing consumer rights training for staff (21%). We have estimated a range of savings based on 3 employees with a time saving of 10 mins to 5 employees with a time saving of 20 mins. The evidence from the IFF survey suggests that many businesses do not train staff on consumer rights on a regular basis and as the new laws will be easier to understand, we believe that savings are based mostly on streamlining the training for new staff, rather than up-skilling existing staff. We have estimated this saving at £0.37m to £1.22m, with a best estimate of £0.79m.

#### *Right to reject limited to 30 days*

119. Limiting the right to reject to 30 days will have three main impacts on business:

- a. It will introduce costs for any firms that currently have a cut-off for refunds for faulty goods of less than 30 days;
- b. It will create direct benefits for businesses that currently offer refunds for faulty goods beyond 30 days, and will no longer have to do so;

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<sup>65</sup> Average annual legal costs are £684 for micros (pop 332,311,) and £23,654 for small, medium and large firms (pop 23,817)

<sup>66</sup> Average annual legal costs are £684 for micro firms (pop 332,311) and £23,654 for small, medium and large firms (pop 23,817)



- c. It will provide clarity in the law, thus reducing the current lack of certainty over whether a refund should be given.

120. Stakeholder engagement with the British Retail Consortium and individual retailers suggested that most retailers currently offer short-term refunds for faulty goods up to 28 or 30 days except in extreme cases<sup>67</sup>. This suggests that there will be minimal impact on most business of clarifying the right to reject period at 30 days. According to the IFF survey responses, the median length of time given for rejection of faulty goods was 1 month<sup>68</sup>, while the mean length of time was 5.1 months.

*a) Costs to business that currently offer less than 30 days*

121. Business will incur costs from the new policy if they currently offer returns for fewer than 30 days. The IFF survey suggests that around two thirds of businesses (approximately 67%<sup>69</sup>) currently offer a right to reject for 30 days or fewer. Based on our overall business population estimate, this would apply to 331,199 micro firms and 24,929 for small, medium and large businesses.

122. Unfortunately the IFF survey does not provide more granular detail of the precise period over which these businesses currently offer a right to reject (i.e. how many days fewer than 30, on average). However, based on consultation responses and discussions with businesses, we consider that:

- Most of these businesses already offer at least a 28-day right to reject period, to ensure compliance with the current law. This was confirmed by consultation responses.
- Most rejections happen within 2 weeks, and virtually all firms offer a right to reject for this time period under the current law. In the majority of cases, a fault will become apparent within two weeks; after this point, it is less likely that a customer will exercise his or her right to reject.

123. For this reason, we consider that the move to a right to reject might lead to a 1 to 2% cost increase, on average, for those businesses currently offering a right to reject of up to 30 days. We consider that this increase takes account of the existing high rate of compliance and the time profile of current returns.

124. According to the IFF survey, the current average annual cost of refunds for businesses, grouped by business size, is £177 for micro and small businesses and £6349 for medium and large<sup>70</sup>. Multiplying this amount by the expected cost increase (1-1.5%) across the population of businesses currently offering up to 30 days right to reject suggests a range of costs to business of £1.45m to £2.18m, with a best estimate of £1.82m per year.

*b. Benefits to business that currently offer more than 30 days*

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<sup>67</sup> Most retailers try to keep the “extreme cases” to a minimum, but they are aware of court cases which found the right-to-reject to last longer than a month in certain circumstances, and if consumers press their cases to reject goods after a month, many retailers say they give way unless they think the claim is fraudulent.

<sup>68</sup> IFF Raw Data Set 2 Table 6/1

<sup>69</sup> IFF Draft Report paragraph 10.7

<sup>70</sup> IFF Stage 2 Cost Sheet Data, F1\_Total

125. Alternatively, there are other businesses that will experience a saving because they currently offer a right to reject period of more than 30 days. The IFF survey suggests that 16% of firms currently offer a right to reject period of between 1 and 6 months, and 17% of firms currently offer a right to reject period of more than 6 months (of which 6% guarantee a full refund for faulty products for over 2 years)<sup>71</sup>. Based on the business population estimates<sup>72</sup>, this suggests that 56,980 businesses offer 1 to 6 months, and 60,542 businesses offer more than 6 months.

126. For the firms currently offering between 1 and 6 months right to reject, we have conservatively estimated a cost saving in the range 1-2% as a result of the change to a 30 day rule. For firms currently offering more than 6 months right to reject, we estimate a cost saving in the range 5-10%, since we would expect a more substantial reduction in the number of payments to consumers. Using the figures for average annual cost of refunds as noted above produces an overall estimate of the benefits to business in the range £2.19m to £4.38m, with a best estimate of £3.29m.

127. Netting the cost and benefits of limiting the right to reject period to 30 days suggests an overall net benefit of £0.74m to £2.20m, with a best estimate of £1.47m per year. This is consistent with consultation responses from business groups which supported fixing the right to reject at 30 days and considered that it would be very beneficial for business.

### *c. Reducing the uncertainty over whether a refund should be given*

128. We believe that limiting the right-to-reject period to 30 days will produce a benefit to businesses and consumers alike by reducing the uncertainty over whether a refund should be given. We have not quantified or monetised this impact separately, as we consider that it is already captured under other impacts including simpler complaint handling and reduced training and legal advice costs for business and under reduced transaction costs for consumers.

## **Benefits to Consumers**

129. We expect that consumers will benefit overall from the proposed reforms for Goods. While we have up-to-date information on consumer detriment, there is not sufficient detail provided to assess the impact of each individual legal change against current sources of detriment. In order to quantify and monetise the consumer impacts, we have assessed two main impacts:

- Transaction and search costs; and
- Risk of consumer detriment.

130. We think that together these two impacts offer a clear and realistic estimate of how the reforms will benefit consumers. The consumer benefit estimates in this section are based on independent research commissioned by BIS into the links between consumer law reform, consumer benefits and economic growth<sup>73</sup>. This research included adapting a model previously used in Australia by the Productivity Commission (APC) which sought to analyse the impact of the simplification of consumer law implemented in 2011. This

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<sup>71</sup> IFF Survey E6, Table 6

<sup>72</sup> BIS Business Population Estimates, 2012: <https://www.gov.uk/government/publications/bis-business-population-estimates>.

<sup>73</sup> Source: ICF GHK 'Consumer rights and economic growth'

approach to assess consumer impacts is common across the Consumer Bill of Rights using figures appropriate to Goods, Services and Digital Content<sup>74</sup>.

### *Reduced transaction and search costs*

131. Consumers with a greater understanding of their rights will have lower search and transaction costs. Transaction costs include those costs which consumers bear to prevent risks such as the cost to consumers of learning their consumer rights. Simplifying consumer law will enable consumers to make better decisions and reduce search time.

132. Transaction costs are difficult to measure accurately in monetary terms and in many cases the greater part of these costs do not cause consumers harm, such as a consumer's search for goods and services that match their preferences. Assuming a conservative estimate of 1%<sup>75</sup> of household expenditure, this equates to transactions costs of £8.6 billion in 2011.

133. This high level estimate would include expenditure outside the scope of changes to consumer law on the supply of goods. Using the earlier methodology (see paragraph 130, footnote 75), it is possible to apportion a share of the transaction costs which would accrue to consumers purchasing goods and is estimated to be £3 billion (35% of £8.6 billion).

134. We estimate that the simplification of consumer law and enhanced consumer remedies will not lead to a large reduction in harmful consumer transaction costs. If we assume a reduction in costs of between 0.5% and 1% the benefit to consumers of goods will be between £14.8 and £29.7 million. In absence of evidence to inform which is the best estimate, the mid point of £22.3 million is chosen as the best estimate. These estimates will increase with the forecast growth in consumption spending which has been estimated using the average long run growth rate in real household expenditure, at 1%.

**Figure 3: Ongoing benefit to consumers from reduced transaction costs: Goods (£ millions)**

	Year									
	0	1	2	3	4	5	6	7	8	9
<b>Best</b>	22.30	22.52	22.75	22.97	23.20	23.43	23.67	23.91	24.14	24.39
<b>Low</b>	14.86	15.01	15.16	15.32	15.47	15.62	15.78	15.94	16.10	16.26
<b>High</b>	29.73	30.03	30.33	30.63	30.94	31.25	31.56	31.87	32.19	32.51

### *Reduced risk of consumer detriment*

135. Consumer detriment exists in the form of the financial cost of problems with goods as well as the lost personal time and emotional distress suffered by consumers. The consolidation and clarification of consumer law and enhancements to consumer remedies will reduce the risk of consumers encountering detriment.

136. The 2012 Consumer Focus Consumer Detriment survey<sup>76</sup> estimated that the annual financial cost to consumers resulting from problems with goods and services was £3.08

<sup>74</sup> Breakdown in business population is Goods 356,128, Service 386,000 and Digital Content 289,000

<sup>75</sup> Source: ICF GHK "Consumer Rights and Economic Growth, page 20 (2013)

<sup>76</sup> Available at: <http://www.consumerfocus.org.uk/publications/consumer-detriment-2012>

billion. This includes the costs incurred by consumers from trying to resolve problems themselves such as seeking legal advice, or replacing the goods affected at the consumer's own expense. Many consumers use their personal time trying to solve consumer problems and using the 2012 Consumer Detriment survey it is estimated that consumers spent 59 million hours dealing with problems. The median hourly wage rate in the UK in 2011 was £11.14<sup>77</sup> giving an estimated cost to the consumer of lost personal time of £660 million per year (£11.14 multiplied by 59 million hrs).

137. The emotional distress from consumer problems can be as significant as the monetary costs to consumers. While it is difficult to accurately value this detriment it has been estimated at 25 – 30%<sup>78</sup> of the value of consumer's financial detriment. The sum of lost personal time, financial detriment to consumers and emotional distress gives a total consumer detriment of £4.7bn to £4.9 billion, accounting for 0.5% of total household expenditure in 2011<sup>79</sup>. This figure represents the objective risk faced by consumers. When they engage in transactions, they face a small risk that they will suffer detriment. An aim of the improved consumer policy framework is to lower that risk.

138. Calculating the gain in reduced consumer risk from the simplification of consumer law and the enhancement of consumer redress is difficult and requires estimation of the future level of household expenditure. The long-run average growth of household expenditure is estimated at 1%, which has been used to forecast future household spending.

139. Finally to estimate the gain to consumers from reduced risk of consumer detriment an estimate of the impact of the reforms on the detriment is needed. The changes are not a significant enhancement of existing consumer rights and so they should have only a limited impact on the detriment avoided, so a conservative reduction in detriment of an estimated 0.5%.

**Formula:**

Gain from reduced risk of consumer detriment = % reduction in consumer detriment from reforms (0.005) x % objective risk to consumers before reforms (0.01) x Forecast household consumption

140. The best estimate for the ongoing net benefit to consumers in the goods market is estimated at £8.32 million initially, and increasing with a 1% increase in household spending.

**Figure 4: The ongoing net benefit to consumers from reduced risk of detriment: Goods (£ millions)**

	Year									
	0	1	2	3	4	5	6	7	8	9
Best	8.32	8.40	8.49	8.57	8.66	8.74	8.83	8.92	9.01	9.10

<sup>77</sup> 2011 Annual Survey of Hours and Earnings, all employees, table 1.4a

<sup>78</sup> Source: Dept BIS Report by ICF GHK "Consumer Rights and Economic Growth, (2013)

<sup>79</sup> Consumer Trends, Household final consumption expenditure, Total Expenditure table 0GSKS. Total household expenditure estimated at £870,679m in 2011.

<b>Low</b>	8.16	8.24	8.32	8.40	8.49	8.57	8.66	8.75	8.83	8.92
<b>High</b>	8.48	8.57	8.65	8.74	8.83	8.92	9.01	9.10	9.19	9.28

## Risks and Assumptions

141. We identified two key risks associated with providing a clearer legal framework for the supply of goods. Firstly, the risk that the revised framework shifts burdens onto business from consumers, or conversely undermines consumer protection. Secondly, a risk that a more certain legal framework removes flexibility in the current law which is relevant to the supply of goods and could therefore disproportionately impact on some traders.
142. In developing these proposals we have sought to mitigate these risks by consulting widely with businesses and consumer groups to identify potential impacts (the Law Commissions consulted in 2008 and BIS consulted in summer 2012), holding workshops with stakeholders on emerging options (September 2012) and informally discussing options with a wide range of goods suppliers and consumer groups. We also commissioned the IFF survey of 1000 retailers which informed our evidence of current provision of redress by traders.

## Alternative Approaches for Micro/Small Businesses

143. We do not propose to exempt micro or small businesses from the new consumer protection regime as this would be detrimental to consumers and other businesses, and would hinder rather than improve market conditions.
144. At the beginning of 2012, micro businesses accounted for 93% of all private sector businesses in the UK<sup>80</sup>. All such businesses are subject to the existing law. To exempt such a large proportion of businesses from the new consumer protection regime would create an even more complex legal regime, with consumer rights varying according to the size of the trader. This would deprive the changes of most, if not all, of their desired clarity and would probably disadvantage the micro-businesses it purported to protect.
145. Consultation responses showed strong and widespread support for applying the consumer protection regime (including the proposals set out in this IA) to all businesses, regardless of size. There was no support for a micro or small business exemption. The reasons respondents gave for supporting the application of a uniform regime across businesses of all sizes were numerous. In particular it was noted that any exemption:
- Would be counter-productive, and detrimental to microbusiness, as consumers would be discouraged from buying from them. Consumers would be encouraged to use large businesses and would be less likely to try out new suppliers, hindering innovation and growth and creating obstacles to market entry<sup>81</sup>
  - Would not encourage business growth, and would cause problems to businesses looking to expand beyond the small business threshold (Trading Standards Institute, Retail Motor Industry Federation)
  - Would allow rogue traders to continue to benefit from the opacity of the current law and might encourage unscrupulous traders to manipulate the way they trade in order to fall into the exemption (Retail Motor Industry Federation, Electrical Safety Council, Which?, Citizens Advice)
  - Would cause confusion among businesses, consumers and enforcers, undermining the aim of achieving a clear and consistent consumer protection regime<sup>82</sup>.

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<sup>80</sup> <http://www.bis.gov.uk/assets/biscore/statistics/docs/b/12-92-bpe-2012-stats-release.pdf>

<sup>81</sup> Response to Consultation - BVRLA, Consumer Focus, Retail Motor Industry Federation, Electrical Safety Council, British Retail Consortium, Ofcom, Citizens Advice, various local Trading Standards Services

<sup>82</sup> Response to Consultation - Co-operative Food, Law Society of Scotland, Consumer Focus, British Retail Consortium, Finance and Leasing Association, Citizens Advice Scotland, Ofcom, Direct Line Group, Bar Council, Citizens Advice, various local Trading Standards Services

## One-in, One-out

146. This measure is in scope of OIOO as it has direct impacts on business. The Government expects the proposed changes to result in an 'IN' of £2.78M. This has been calculated on the basis of best estimate calculations on impacts which are direct and in scope for businesses as follows:

### Costs:

- One-off familiarisation costs for business of £2.40m;
- Transitional, one-off legal advice costs of £5.71m;
- Limiting tier 1 to 1 repair/replacement costs of £2.17m
- Cost of amending deduction for use arrangements of £0.96m
- Cost of increase in the number of complaints received from consumers of £0.46m per year
- Cost of increase in consumer redress £5.71m.

### Benefits:

- Time savings from simpler complaint handling of £1.48m per year;
- Savings from reduced number of cases escalating to a court case of £1.22m per year;
- Savings in ongoing legal advice costs (after transition) of £2.45m per year;
- Savings from reduced training costs of £0.79m per year
- Savings from change to right-to-reject period for businesses currently offering above 30 days of £1.47m per year.

147. Over the life of this measure there are direct annual costs of £10.2m and direct annual benefits of £7.5m accruing to business, netting to an IN of £2.78m (Equivalent Annual Net Cost to Business).



## **Annex A: Detailed outline of preferred option (compared to existing law)**

### **A. Right to Reject**

1. Currently, consumers can reject (and obtain a refund for) goods which are faulty at the time of purchase until they have ‘accepted’ those goods. Acceptance of bought goods is determined by whether the consumer has either acted on the goods in a manner inconsistent with the seller's ownership of the goods (e.g. by altering the goods), or retained the goods beyond a ‘reasonable time’, without intimating to the retailer that they reject them.
2. What constitutes a ‘reasonable time’ depends on the circumstances, making it difficult for consumers and businesses to know for how long after supply a refund must be given.
3. The key objective is to improve clarity for both consumers and traders as to when the right to reject may be exercised. Therefore, we propose to set a fixed period of 30 days for the right to reject faulty goods, with an exception only where goods are perishable and would not be expected to last 30 days.
4. A further objective is to promote repair and replacement as viable alternatives to rejection. As a result, where a consumer opts for a repair or replacement within 30 days of purchase, we propose to suspend the period for rejection for the duration of any repair work or the delivery of a replacement, so as not to disincentivise repair or replacement.

### **B. Tier 1 Remedies – repairs and replacements**

- Repair and replacement are forms of redress for faulty goods provided under EU Directive 1999/44, which has been enacted into domestic UK law: a consumer can require repair or replacement of a good which was faulty at the time of purchase (Tier 1)<sup>83</sup>. These remedies seek to correct the fault and keep the contract between the trader and the consumer alive.

### **C. Tier 2 Remedies – reduction in price or reject/refund**

5. In some circumstances (see below), the consumer can keep the goods and receive reimbursement of some of the price paid, or reject the goods and get a refund (known as rescission). These ‘Tier 2’ remedies also derive from Directive 1999/44.
6. There are two areas of ambiguity in the law at present around how Tier 1 and 2 remedies work.
  - i). At present, the consumer can only insist on a Tier 2 remedy if the Tier 1 remedies are impossible or a Tier 1 remedy has not been provided within a ‘reasonable time’ or without ‘significant inconvenience’. To provide more certainty as to when a consumer may insist on a Tier 2 remedy, we propose a limit of one repair or one replacement, after which a consumer can require a Tier 2 remedy. To this end there will be 4 criteria, at least one of which must be met before the consumer may insist on a second tier remedy. The third and

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<sup>83</sup> Except where the consumer's choice is ‘impossible or disproportionate’ (in which case it moves to the alternative, or ‘Tier 2’).

fourth criteria are present under the current law (and derive from the Consumer Sales and Guarantees Directive):

- If the retailer has made an attempt to repair the goods in order to bring them in line with the quality standards but the goods still fail to meet those standards; or
- If the retailer has provided replacement goods (as the original goods did not meet the quality standards) and these also fail to meet the standards; or
- If the consumer has required the retailer to repair or replace the goods, but the retailer has failed to do so within a reasonable time and without significant inconvenience to the buyer; or
- The consumer is unable to insist on a first tier remedy because both options are impossible.

ii) If a tier 2 refund is required, the business may make a deduction to take account of the consumer's use of the good. There is currently no limit or guidance on the amount of the deduction.

7. Our primary policy objective is to provide clarity. We propose that where a business provides a refund under this scheme, they cannot normally make any deduction for the consumer's use of the good within the first six months. Thereafter, the trader may deduct an amount to take account of the consumer's use. This balances the interests of consumers who may have had limited and/or problematic use of the goods and the interests of businesses to not be obliged to compensate consumers beyond what goods are worth.
8. We have considered that in some cases, consumers will have lost the right-to-reject faulty goods where they may have been able to reject beyond 30 days under the current law. We have sought to balance the benefit of that policy to business with the guarantee to the consumer of a full refund, if the goods fail to meet the required quality standard and the repair/replacement provided fails to solve the problem within six months from purchase.
9. We considered six months an appropriate time within which to oblige businesses to provide a full refund under tier 2 because this was the period set out in the consultation proposal that met with the greatest support from respondents. Additionally, there is a legal presumption, in relation to the 1<sup>st</sup> and 2<sup>nd</sup> tier remedies, that a fault in goods which manifests within six months from purchase was present at the time of purchase. After that point, the law requires that the consumer prove that the fault was present at purchase in order to pursue the tier 1 or 2 remedies. Setting a six-month period in relation to the deduction for use would minimise the number of different timescales in operation within the new legislation.

#### *Deterioration in Value of High Value Goods*

10. A secondary policy objective is to minimise undue costs to retailers in industries where goods deteriorate in value rapidly after purchase. Therefore, where robust, independent evidence of the second hand value of the class of goods exists, the retailer can make a deduction for use, even during the first six months, provided the refund is of at least that second hand value. We intend to state in guidance that it may be beneficial for industries that intend to rely on such evidence to seek an independent 'accreditation' of the evidence.
11. Businesses in the Motor Vehicles & Parts industry tend to offer repairs more frequently than other goods sectors surveyed, with the majority of even small businesses carrying out

repairs on goods between 20 and 49 times in the last twelve months<sup>84</sup>. Furthermore, 21% of Motor Vehicles & Parts businesses would seek to repair a faulty good a second time, compared to 11% of goods retailers generally<sup>85</sup>. While this figure includes both the sale of vehicles and their constituent parts, we expect those selling vehicles, in particular, to carry out more repairs of a persistently faulty good, based on comments made by the Retail Motor Industry Federation and others, in their consultation responses<sup>86</sup>. That is to say, motor retailers are both more likely to seek to repair a faulty good, and to carry out additional repairs, rather than refund or compensate the consumer. Therefore, these proposals will have the greatest costs for them.

#### D. A Single Scheme of Remedies

12. Traders may supply goods to consumers under a variety of ‘contract types’. Currently, there is a lack of consistency around the forms of redress available to consumers, if their goods are faulty, depending on the type of contract involved.

13. The different contract types are as follows:

- Sale - goods exchanged for money in the familiar way
- Conditional Sale - sale where the consumer pays in instalments and only obtains ownership of the goods when he makes the final payment, although he may use the goods in the meantime
- Barter or Exchange - goods exchanged for something other than money
- Work & Materials - goods supplied as part of a contract for work or services
- Hire Purchase - a hire contract with an option to buy at the end of the hiring period
- Hire - a hire contract with no intention that the consumer will obtain ownership of the goods

14. The table below illustrates the different remedies that apply to these contract types.

Contract Type	Remedies Available (where goods are not of satisfactory quality, or do not correspond with description or sample, or are not fit for a known purpose)		
	Right to Reject	Damages	1 <sup>st</sup> & 2 <sup>nd</sup> tier (EU-derived remedies)
Sale	Short-term	Yes	Yes
Conditional Sale	Long-term	Yes	Yes
Barter or Exchange	Long-term	Yes	Yes
Work & Materials	Long-term	Yes	Yes
Hire Purchase	Long-term	Yes	No
Hire	Long-term	Yes	No

15. The policy objective is to provide a clearer, simpler and more accessible framework of remedies for faulty goods, facilitating better consumer and retailer awareness of their rights and obligations in each situation. We therefore propose that the short-term right-to-reject of 30 days and tier 1 and 2 remedies should apply for all contracts where a business supplies goods to a consumer

<sup>84</sup> IFF Raw Data Table 19/3

<sup>85</sup> IFF Raw Data Table 21/1

<sup>86</sup> Response to Consultation – RMI, 7, Q12

16. However, in hire contracts, because the consumer pays for use, and the ownership of the goods is not transferred, the consumer will not be entitled to claim back any payments made for any hire period that they have already had.
17. The intention is to apply the short-term right to reject to all contract types, rather than the long-term right, as the short-term right is robust, commonly used and well regarded by both consumers and businesses<sup>87</sup>. On the other hand, the long-term right to reject could be more costly to business than a limited short-term right and applying this to all contract types would be out of line with the evidence of what many businesses already offer for sales of goods. The long-term right can be less straightforward, in that if the consumer has derived any use from the goods (which is likely in the majority of such cases) then the consumer may not be entitled to full reimbursement (though in some cases the Courts have awarded reimbursement). It was suggested in the Law Commissions' consultation that there is less awareness among consumers of the long-term right<sup>88</sup>. As such the long-term right does not provide the certainty and clarity of the short-term right.

### **E. Expressing Rights More Clearly**

18. Currently, where a consumer buys goods from a business, the law implies that the business makes a set of promises to the consumer about those goods, even where the business does not say anything, or says something to the contrary. These promises are referred to in the legislation as "implied terms" and classified as "conditions" and "warranties". The terms range from the business having the right to sell the goods and will not disturb the consumer's use of them, to terms about what the goods should be like. These latter terms about the condition of the goods include that they: match the description they were sold under, are of satisfactory quality, and are fit for purpose. These "implied terms" are what we mean by 'consumer rights'. The classification of each right as either a condition or warranty indicates that it is a contractual promise and also determines the remedies available if it is breached (a breach of a condition triggers an additional remedy – termination of contract - to a breach of warranty). This way of setting out the rights (and indicating remedies) is inaccessible and confusing for consumers.
19. The policy objective is that a consumer facing a problem with goods that they have been supplied with, should be able to see clearly from the Act that results from these proposals what their rights are and what remedies are available if the business does not fulfil these rights. These rights will continue to be enforced as contractual terms (i.e. by a claim for breach of contract) but interpretation will be easier than at present.

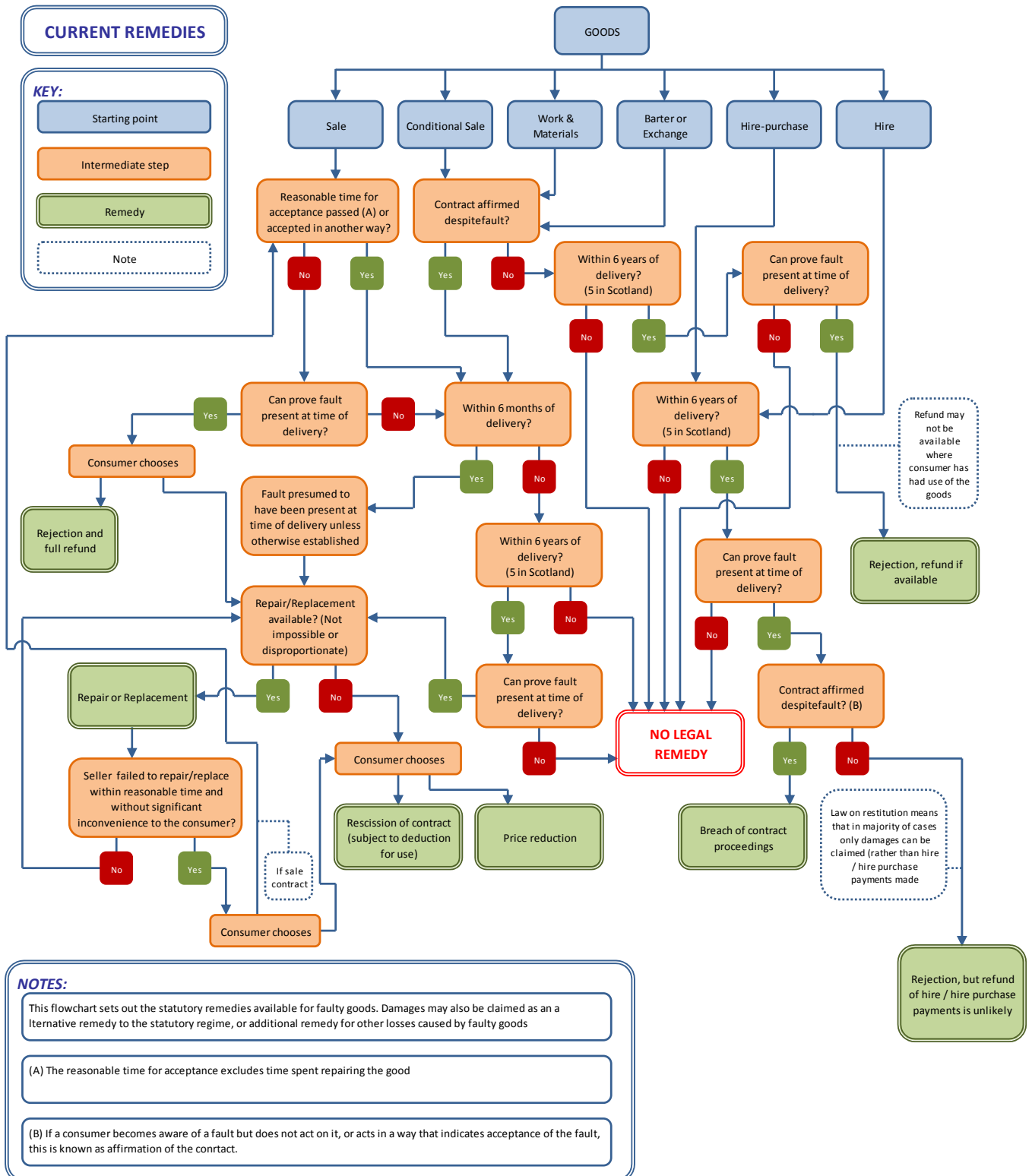
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<sup>87</sup> See the Law Commission & Scottish Law Commission (Law Com No 317, Scot Law Com No 216), pages 21-8.

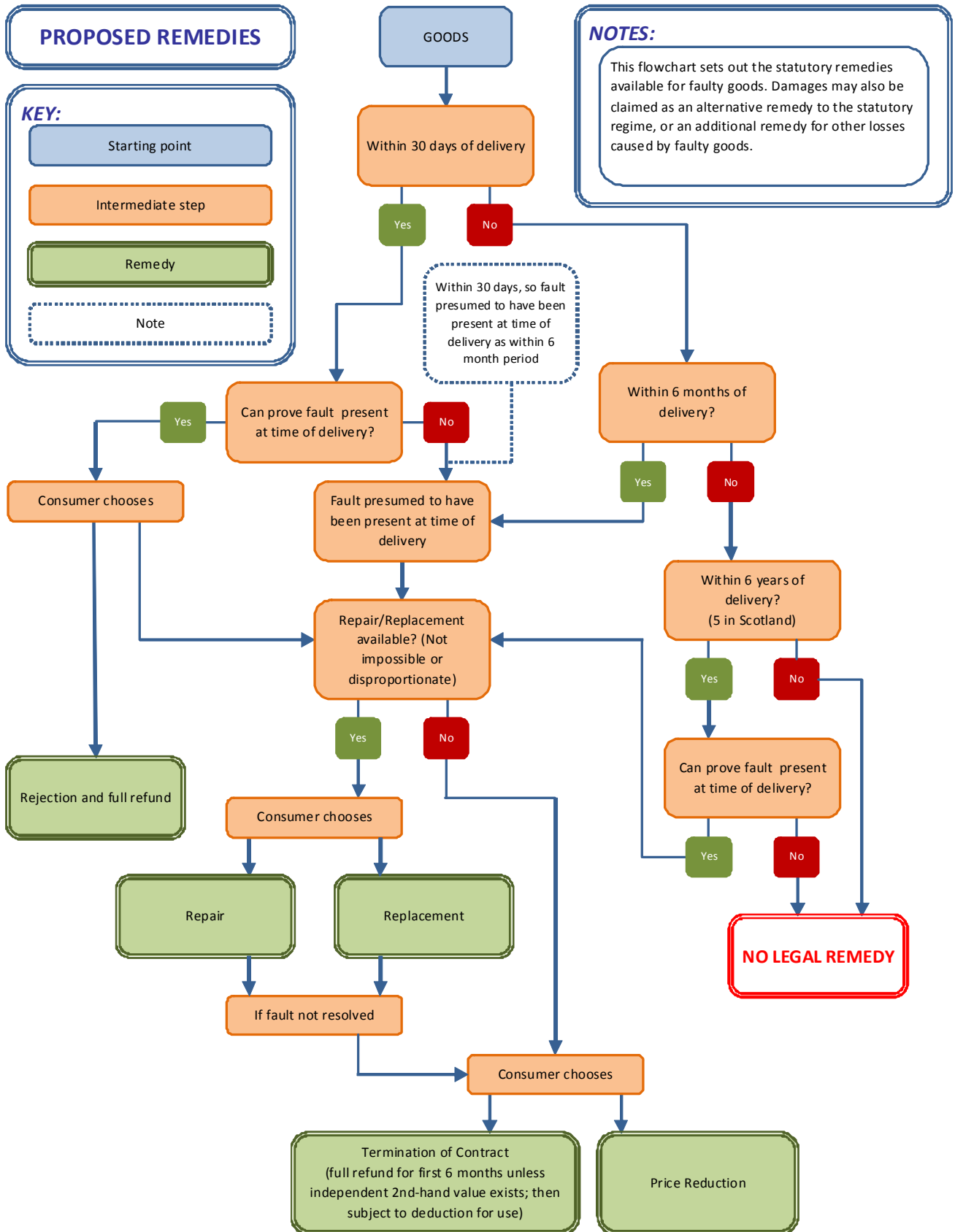
<sup>88</sup> Ibid, paragraph 5.10.

# Annex B: Flowcharts of Current & Proposed Remedies For Goods

## Figure 2: Flowchart of Current Remedies for Faulty Goods



**Figure 3: Flowchart of Proposed Remedies for Faulty Goods**



## Annex C: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. If the policy is subject to a sunset clause, the review should be carried out sufficiently early that any renewal or amendment to legislation can be enacted before the expiry date. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below

**Basis of the review:**

This Impact Assessment includes a commitment to review the proposed changes 3-5 years after implementation.

**Review objective:**

To assess:

- the level of take-up of new scheme of remedies
- whether the policy changes are meeting policy objectives
- whether policy objectives are in practice feeding through to increased consumer empowerment.

**Review approach and rationale:**

The review would evaluate the effectiveness of the changes within this Impact Assessment. The review will incorporate stakeholders' views that will include consumer groups, business groups, Local Authority Trading Standards Services, the Consumer and Markets Authority (CMA) and the Citizens Advice services.

**Baseline:**

Total detriment suffered by consumers has been estimated at £3.08 billion per year. This results from a wide variety of consumer problems including faulty and defective goods, and failure and delay in repairs.

**Success criteria:**

Increased consumer empowerment, reduction in consumer detriment, reduced disputes including court cases.

**Monitoring information arrangements:**

Feedback from businesses, consumers groups, Trading Standards Services, the CMA and Citizens Advice will be achieved through regular engagement. The transition costs will be recorded during the implementation stage and Government will monitor the ongoing costs via annual reports and management information.

More general information about the impacts on business from the proposed changes will be collected from business groups and through surveys.

**Reasons for not planning a review:**

N/A

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