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The United Kingdom's responsible lending rules have provided stronger protection for consumers through the exclusion of the financially vulnerable, how can the responsible lending practices strengthen the financially vulnerable consumer's access to credit?

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Have the FCA provided regulations which effectively protect the financially vulnerable from harmful practices?

Introduction

Following on from the global financial crisis in the United Kingdom (UK), regulation and supervision of financial businesses has been reformed significantly.[1] As a direct result of the financial crisis, the payday loan market grew at a rapid pace, with millions of families struggling to deal with stretched incomes and firmer restrictions on mainstream credit.[2] This resulted in many turning to high-cost short-term credit, to survive such changes, payday loans being the primary alternative to mainstream credit.[3]

Payday lending in the UK however, has attracted vast amounts of negative political and media attention from the issues that have arisen in the consumer credit industry.[4] Concerns were raised by consumer groups, debt-advice charities and other interested parties regarding the operation of the payday lending sector.[5] Poor and irresponsible lending practices, product features and the high cost of the repayment of such loans led to a vast amount of people falling into severe financial difficulties.[6] High-cost short-term credit firms,

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[1] Andrea Fejos, '*Achieving Safety and Affordability in the UK Payday Loans Market'* (2015) 181 >https://moodle.essex.ac.uk/pluginfile.php/706335/mod_resource/content/1/Fejos%2C%20Payday%20loans%2C%20official%20copy.pdf <accessed 21 May 2019

[2] ibid

[3] Laura Rodrigues, *'Payday loans: The next generation: Changes to the high-cost short-term credit market since the introduction of the price cap'* (StepChange Debt Charity Report, 2016) 2 > https://www.stepchange.org/Portals/0/documents/Reports/Payday-loans-next-generation.pdf <accessed 21 May 2019

[4] Competition and Markets Authority, *'Payday lending market investigation: final report'* (2015) 28 >https://assets.publishing.service.gov.uk/media/54ebb03bed915d0cf7000014/Payday_investigation_Final_report.pdf <accessed 22 May 2019

[5] ibid

[6] Rodrigues (n3) 2

credit lenders particularly in the payday lending industry, have caused numerous problems for consumers.[7] Unregulated and unscrupulous practices carried out by these credit lenders have caused an alarming level of debt for their consumers and generated a widespread level of harm and misery.[8] These unscrupulous practices include a variety of issues, such as the firms not properly assessing a customers affordability to meet the repayments due on a loan, not being thorough in their checks and asking potential borrowers for very little of information and no proof.[9] Further issues include inappropriate and misleading advertisements, and whether forbearance is shown when customers get into difficult meeting repayments.[10]

Research has shown that approximately one in six people with consumer credit debt suffer moderate to severe 'financial distress', which has led to them experiencing financial difficulties or other issues such as mental health problems, caused by the strain of repaying their debts.[11] Widespread concerns regarding the credit products being sold and practices of payday lenders lead to the introduction of the Financial Conduct Authority (FCA) and stricter rules on payday lending.[12] The government acknowledged that intervention was prominent and was needed to address such problems, thus, when the FCA gained the ability to regulate and supervise consumer credit, it prioritised and focused on payday loans.[13] In 2013, the FCA proposed a regime which aimed at providing stronger protection consumers in the UK,

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[7] Citizens Advice, *'Payday Loans after the cap: are consumers getting a better deal?'* (2016) 9 > https://www.citizensadvice.org.uk/Global/CitizensAdvice/Debt%20and%20Money%20Publications/Payday%20Loan%20Report%202.pdf <accessed 22 May 2019

[8] ibid

[9] ibid

[10] Competition and Markets Authority (n 4) 28

[11] Financial Conduct Authority, '*Preventing financial distress by predicting unaffordable consumer credit agreements: An applied framework'* (Occasional Paper 28, 2017) 3 > 21 May 2019 https://www.fca.org.uk/publication/occasional-papers/op17-28.pdf <accessed

[12] Rodrigues (n 3) 2

[13] Fejos (n 1) 182

through tougher requirements for payday lenders including a mandatory affordability assessment.[14] These new responsible lending rules have calmed the storm, the regulations and guidance given to credit lenders has prevented such financial companies from carrying out bad practices, and whilst the FCA has generally done well in providing rules and guidance, there is good reason to believe that the actions of the FCA have gone some way to tackling the worst excesses of the payday loan market.[15] Although one would argue that this is welcomed progress, there is still a long way to go before these rules fully protect consumers.

The primary aim of this research is to identify any flaws in the current FCA responsible lending rules, and secondly to find alternatives for the financially vulnerable to access credit, deciphering whether strengthening consumer protection or providing for better alternatives is the way forward for effective consumer protection. This essay will proceed to demonstrate how the UK's responsible lending rules have provided stronger protection than before for consumers, however strengthened consumer protection has limited access to credit. Providing stronger consumer protectionist measures is likely to exclude the financially vulnerable sector of society, yet the current measures in place provide too much scope for credit lenders, which allows them to abuse the measures the FCA have put in place, and subsequently lead to the financially vulnerable not getting the level of protection they deserve.

[14] Financial Conduct Authority, '*The FCA sets out in detail how it will regulate consumer credit, including payday lending, when it takes over responsibility in April 2014*' (Press Release, 2013) >https://www.fca.org.uk/news/press-releases/fca-sets-out-detail-how-it-will-regulate-consumer-credit-including-payday <accessed 21 August 2019

[15] Rodrigues (n 3) 5

High-Cost Short-Term Credit and the Payday Loan Industry

In order to discuss high-cost short-term credit and the payday loan industry, the first points to establish are what is high-cost short-term credit? And specifically, what are payday loans? Research shows that the UK is home to the second largest payday lending market in the world, closely followed by the United States with approximately 10% of the UK adult population having applied for a payday loan, this being approximately 4.6 million adults.[16] Whilst the UK's consumer credit market one of the biggest in Europe, it experiences rapid changes on a recurrent basis.[17] The market includes an array of products, ranging from mainstream credit, such as personal loans and credit cards, to high-cost short-term credit such as the payday lenders who offer short-term loans to consumers, subject to an interest rate.[18]

This type of credit is regularly used by consumers, however, different types of people use this credit for very different reasons to give an example, many may use credit to manage finances whilst others may use it to buy luxury items, such as taking out a personal loan to purchase a car.[19] One consumer may participate in this market very differently to the next. However, many consumers participate in this market due to mainstream credit being inaccessible, whether it be due to a poor credit history or a low income.[20] Therefore, these consumers are different to those who use the credit for luxury items, they participate in this

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[16] John Gathergood, Benedict Guttman-Kenney, Stefan Hunt, '*How Do Payday Loans Affect Borrowers? Evidence from the UK Market'* (Oxford University Press, 2018) 497 >https://0-watermark-silverchair-com.serlib0.essex.ac.uk/hhy090.pdf <accessed 22 July 2019

[17] National Audit Office, '*Office of Fair Trading: regulating consumer credit'* (2012) 9 >https://www.nao.org.uk/wp-content/uploads/2012/12/1213685.pdf <accessed 03 July 2019

[18] ibid

[19] ibid

[20] National Audit Office (n 17) 12

market to carry on with day to day necessities, to purchase items that are essential to them in everyday life.[21]

The high-cost credit market is older than money itself, however, when discussing this market it is practicable to ask, what exactly does high-cost credit really mean?[22] Precisely defining payday lending is difficult due to the complexity of the market, and the links it has to other forms of fringe finance.[23] These links and relationships with other financial products, such as the ones given as examples above, have created an unexpected level of controversy in the UK.[24] Whilst this is the case, the FCA decided upon its own terminology and definition for this specific type of credit product.[25] High-cost credit refers to high interest, short-term loans from finance companies who aim to make a profit from the interest charged to the consumer on the loan.[26] One of the more flagrant and costly traps that low income or vulnerable individuals are compelled to step into, is that of payday loans.[27] Payday loans are a form of high-cost credit, usually for small amounts of money, which can be repaid over a short period of time.[28] It was tradition that the repayment for the loan would be paid on the customers next payday, hence the term payday loan,

[21] ibid
[22] Christopher L. Peterson, '*Taming the Sharks: Towards a Cure for the High cost Credit Market*' (1st edn, University of Akron Press, 2004) 45
[23] Karen Rowlingson, Linsey Appleyard, Jodi Gardener, 'Payday lending in the UK: the regul(aris)ation of a necessary evil?' Cambridge University Press 45(3) (2016) 531 >https://0-www-cambridge-org.serlib0.essex.ac.uk/core/services/aop-cambridge-core/content/view/FF33B00EC7A0087283BDE8092397A824/S0047279416000015a.pdf/payday_lending_in_the_uk_the_regularisation_of_a_necessary_evil.pdf <accessed 26 July 2019
[24] ibid
[25] Karen Fairweather, Paul O'Shea, Ross Grantham, *'Credit, Consumers and the Law: After the global storm'* (Routledge, 2017) 133
[26] ibid
[27] Carol Realini, Karl Mehta, '*Financial Inclusion at the Bottom of the Pyramid*' (1st edn, FriesenPress, 2015) 28
[28] Fejos (n 1) 182

however many are now repayable over longer periods of time, across several months for example,[29] furthering away from the notion of 'short-term'.

Why is consumer protection important?

Following on from the financial crisis of 2008, the payday lending market experienced a significant growth.[30] The market has evolved into an environment where individuals find themselves in a situation of financial disarray where cash is needed instantly, for a short period of time, and where mainstream credit is inaccessible to them.[31] Whilst the market has very gradually declined in recent years, the volume and amount lent today is still considerably high.[32] Whilst many of the loans are for small amounts, an average being estimated at two hundred and sixty pounds, the issue arises from the inexistent financial ceiling on the size of the short-term loan.[33]

It is apparent that today too many low-income families are turning to payday loans as a safety net to survive, relying on them to pay for everyday household items, or one-off expenses that are immediately unaffordable.[34] It was estimated that 1.4 million people used high-cost credit in 2017 for everyday household costs, a rise above the 1.1 million calculated in 2016.[35] This regular reliance on such credit put pressure on households who are already

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[29] ibid

[30] Anu Aurora, 'Payday loans: filling the gaps in the short-term loan market' (Company Lawyer, 2017) >https://login.westlaw.co.uk/maf/wluk/app/document?&srguid=i0ad629030000016bbc32f9905c3e33f9&docguid=I70DF77A03A1F11E7A9E1F8E5C12DC658&hitguid=I70DF77A03A1F11E7A9E1F8E5C12DC658&rank=10&spos=10&epos=10&td=60&crumb-action=append&context=6&resolvein=true <accessed 04 July 2019

[31] ibid

[32] Alexander Hill Smith, *'Money, Money, Money'* 165 NLJ 7651 (2015) 15 > https://0-www-lexisnexis-com.serlib0.essex.ac.uk/uk/legal/results/enhdocview.do?docLinkInd=true&ersKey=23_T28888326158&format=GNBFULL&startDocNo=0&resultsUrlKey=0_T28888326160&backKey=20_T28888326161&csi=280276&docNo=5&scrollToPosition=343 <accessed 14 July 2019

[33] ibid

[34] Rodrigues (n 3) 2

[35] ibid

on very tight budgets and leaves them particularly vulnerable to falling into problem debt.[36] It is clear to see that payday loans are still very common today, and their popularity leaves one to question whether the regulations put in place by the FCA suffice to meet consumer protection standards and prevent issues such as spiralling debts for consumers who cannot afford to repay these loans. As consumer protection is vital to this research, the question that arises is why is consumer protection so important? Why should consumers be protected?

The economic recovery, following the recession in the UK, has started to show signs of improvement, with economic growth gradually increasing.[37] However, the benefits of such recovery are being disproportionately felt by the UK population, with the most advantaged feeling the majority of its benefits.[38] Research demonstrates that millions of people and families in the UK are still struggling with their everyday financial affairs, food, water and electric bills to give examples.[39] Fifteen million people falling behind on their bills, including six million who use credit to keep going until payday, alongside three million people who use credit to maintain their already existing credit commitments.[40] In 2013 it was reported that nine of the UK's biggest payday lenders saw their turnover double in the previous three years, with one firm recording a thirty-two fold increase in profits since the beginning of the recession in the UK.[41] A big player in the payday lending market, Wonga, reported record profits, a 36% increase on the previous year.[42] Whilst Wonga claimed its profits were not

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[36] ibid
[37] Fairweather, O'Shea, Grantham (n 25) 134
[38] ibid
[39] ibid
[40] ibid
[41] Meghna Mukerjee, '*It's Been a Good Year for Wonga: That's Never a Good Sign'* (NewStatesman, 2013) > https://www.newstatesman.com/business/2013/09/its-been-good-year-wonga-thats-never-good-sign <accessed 10 August 2019
[42] ibid

from preying on people living on the breadline, being desperate, the firm was heavily criticised for generating profit from low income consumers forcing them into misery and pushing the needy deeper into debt.[43] Historically, it was not in a lenders best interest to engage in unscrupulous lending practices. However, firms used sophisticated television advertisements, for a consumer it would have been hard to avoid the lure of the 'quick and easy' payday loan.[44] Further, a number of changes to the consumer credit market caused lending standards to fall, which has subsequently led to the rapid rise of irresponsible lending.[45] This rise in irresponsible lending is the primary reason consumer protection has been highlighted and emphasis has been placed on its importance.[46] Nearly 93% of people believed that regulation was needed, topping public concern was the advertising of payday loans, and the need to give a clearer indication about the total cost of the debt, overall consumers needed to be educated about payday loans and regulations needed to prevent such harmful practices.[47]

The central focus of contemporary consumer economies is credit, and it is therefore unsurprising that governments should demonstrate a great level of concern when promoting and regulating its use.[48] However, there are very specific reasons as to why consumer protection is such an important aspect of regulating credit. It is apparent that many consumers use high cost short term credit as part of their everyday lives without

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[43] ibid

[44] R3, *'The Association of Business Recovery Professionals, 'Rein in "Payday Lenders," Say 93 Percent of GB Population'* (press release, 2012) > www.r3.org.uk/index.cfm?page=1114&element=16322 >accessed 10 August 2019

[45] Jessica Tuffin, '*Responsible Lending Laws: Essential Development or Overreaction*' Queensland University of Technology Law and Justice Journal 9(2) (2009) 281 >https://0-heinonline-org.serlib0.essex.ac.uk/HOL/P?h=hein.journals/qutlj9&i=287 <accessed 26 July 2019

[46] ibid

[47] R3 (n 44)

[48] Iain Ramsay, *'Consumer Law and Policy: Text and Materials on Regulating Consumer Markets'* (3rd edn, Hart Publishing, 2012) 361

running into serious difficulties, however this is not always the case, many consumers fall into harmful debt traps.[49] Whilst payday loans offer a quick fix for consumers to get money instantly, and although there are benefits to an increased availability of credit, which will be discussed further in the next section, this availability has been overshadowed by a 'dark side' to consumer credit.[50] This so called 'dark side' is shown through increased record levels of consumer debt and evidence of continuous irresponsible lending practices.[51] Longstanding claims have been made by consumer and welfare organisations in the UK, that payday lending has detrimental effects on financially vulnerable consumers, those consumers who are a primary target for the payday lenders.[52] The debt support trust found that whilst assisting people with their financial woes, most people found themselves to be struggling in other areas of their life as a direct result of debt, be it marital issues, mental health issues or problems at work.[53] Research has found that a relationship exists between debt and maternal depression among lone parents, further debt has formed a relationship with stress, anxiety and depression.[54] Consumer protection has gradually developed over the past few decades and from this general field emanated specific principles, one of which was financial consumer protection.[55] The global financial crisis of 2008 emphasised the

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[49] National Audit Office (n 17) 5

[50] Abdul Karim Aldohni, '*Law and Finance after the Financial Crisis: The Untold Stories of the UK financial Market'* (Routledge, 2017) 50

[51] ibid

[52] Paul Ali, Cosima McRae, Ian Ramsay, '*Payday lending regulation and borrower vulnerability in the UK and Australia*' JBL (2015) >https://login.westlaw.co.uk/maf/wluk/app/document?&srguid=i0ad629030000016bb9d63abb49d207bf&docguid=IE127E150D99111E4A980CA5F572AE19A&hitguid=IE127E150D99111E4A980CA5F572AE19A&rank=27&spos=27&epos=27&td=1928&crumb-action=append&context=17&resolvein=true <accessed 03 July 2019

[53] Stuart Carmichael, *'Borrower Beware',* Pay and Benefits (9)(2015) >https://0-www-lexisnexis-com.serlib0.essex.ac.uk/uk/legal/results/enhdocview.do?docLinkInd=true&ersKey=23_T28888075895&format=GNBFULL&startDocNo=0&resultsUrlKey=0_T28888082654&backKey=20_T28888082655&csi=280242&docNo=3&scrollToPosition=332 <accessed 14 July 2019

[54] Ramsay (n 48) 468

[55] P. O'Shea, K. Fairweather, R. Grantham, '*Credit, Consumers and the Law: After the Global Storm'* Journal of International Banking Law and Regulation (2017) >https://login.westlaw.co.uk/maf/wluk/app/document?&srguid=i0ad8289e0000016b8dbc2c565d6eeec1&doc

importance of the doctrine of financial consumer protection, highlighting why this field needed to be regulated, looking at consumer credit in particular.[56]

The financially vulnerable sector of society- who are they and why should they be protected?

It has already been established that many consumers participate in the payday lending industry due to mainstream credit being unavailable, whether it be due to a poor credit history or low income. These consumers are different to those who use payday loans for luxury items. Whilst both types of consumer should be protected, extra protection is needed for the latter who use them due to the lack of access to mainstream credit. The main question which is pivotal to the discussion this research will portray is who are the financially vulnerable and why should they be subject to strict regulations that protection them as a credit consumer?

As the term financially vulnerable will be used a lot throughout this research, it is important to decipher what is meant by this term. Whilst the Oxford Dictionary provides that the adjective 'vulnerable' means to something or somebody weak and easily hurt physically and emotionally, its definition is far from this simple.[57] The FCA identified that the term vulnerability is so subjective it makes the term hard to define,[58] however, the majority of consumers who use consumer credit may be vulnerable to a certain degree due to their financial circumstances.[59] The FCA considered a vulnerable consumer to be someone who,

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guid=I74E3B1407C4B11E7A2C08479636B414E&hitguid=I74E3B1407C4B11E7A2C08479636B414E&rank=12&spos=12&epos=12&td=57&crumb-action=append&context=6&resolvein=true <accessed 25 June 2019

[56] ibid

[57] 'vulnerable' Oxford Dictionary (3rd edn, Oxford University Press, 2010)

[58] Financial Conduct Authority, *'Consumer credit and consumers in vulnerable circumstances'* (2014) 5 > https://www.fca.org.uk/publication/research/consumer-credit-customers-vulnerable-circumstances.pdf <accessed 09 August 2019

[59] ibid

due to their personal circumstances, is especially susceptible to detriment.[60] Whilst this definition is provided, the category is very broad, and to effectively protect consumers, one would suggest that the specific categories of people who fall within this definition need to be identified. When classifying the financially vulnerable, a large variety of factors must be taken into consideration which makes defining this category very difficult. It is apparent that addressing the issue of financial exclusion is a key UK European objective, with the Treaty of Lisbon embodying the reduction of social exclusion.[61] However, in terms of credit, one would say that a financially vulnerable consumer can fall in to many sub categories and whilst one consumer may constantly be classed as financially vulnerable, another may fall into this category for a temporary period of time. In the context of finance, vulnerability is important and whilst being on a low income is not a sole or necessary condition of vulnerability, it is a cause of financial vulnerability, and combined with others such as young age or simply lacking a level of literacy, can cause this consumer significant harm.[62] The House of Commons Treasury Committee broadly welcomed the FCA's work to define vulnerability and identified that the FCA's broad definition of vulnerability enables it to incorporate those who may experience these circumstances occasionally and be classified as vulnerable for a temporary period of time, as well as those individuals who may be permanently vulnerable.[63]

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[60] ibid

[61] Ramsay (n 48) 498

[62] Abdul Karim Aldohni, *'The UK New Regulatory Framework of High Cost Short Term Credit: Is There a Shift Towards a More "Law and Society" Based Approach?'* (J Consum Policy, 2017) 325 > http://content.ebscohost.com/ContentServer.asp?EbscoContent=dGJyMMTo50Seprc4v%2BvlOLCmr1Gep7RSsam4SLCWxWXS&ContentCustomer=dGJyMPGvtkmyqLdNuePfgeyx9Yvf5ucA&T=P&P=AN&S=R&D=bsu&K=124971272 <accessed 09 August 2019

[63] House of Commons Treasury Committee, *'Consumer's access to financial services'* (29th report of session, 2019) 51 > https://publications.parliament.uk/pa/cm201719/cmselect/cmtreasy/1642/1642.pdf <accessed 12 August 2019

To build upon the FCA's definition, the individual categories will be explored, which will allow one to determine whether they are covered by the consumer protectionist measures the FCA have put in place. Firstly, it is apparent that those who have experienced or currently possess a poor credit history can be subject to this category, financially vulnerable consumers may be classified at those who experience financial difficulty, are currently in debt or who experience financial problems on a daily basis.[64] In the past, evidence has suggested that many consumers who had decided to turn to payday lending had experienced financial problems, with many of these having had an unauthorised overdraft and many more having experienced a debt problem in the years prior to applying for a payday loan.[65] Further, research has found that consumer credit firms prioritised the repayment of a loan over the consumers circumstances, which generated widespread evidence of poor customer outcomes.[66] Many consumers had poor credit histories and restricted access to other forms of credit which meant that some consumers are likely to have been less price sensitive.[67] It is practicable to say that providing credit to consumers who have struggled with finance in the past is simply opening the door to a debt trap that the consumer is unaware of, further if the consumer does not have access to mainstream credit, should they be allowed to enter into these high interest loans?

[64] ibid
[65] Aurora (n 30)
[66] Caroline Binham, *'Widespread evidence of poor outcomes at consumer-credit firms'* Financial Conduct Authority (2016) >https://moodle.essex.ac.uk/pluginfile.php/615878/mod_resource/content/1/Binham%2C%20%E2%80%98Widespread%20evidence%E2%80%99%20of%20poor%20outcomes%20at%20consumer-credit%20firms%20%E2%80%93%20FCA.pdf <accessed 23 May 2019
[67] Office of Fair Trading, '*Payday Lending, Final Decision on Making a Market Investigation Reference'* (2013) 7 >https://assets.publishing.service.gov.uk/media/532ad579e5274a226b000307/payday-MIR.pdf <accessed 23 May 2019

There is a further acknowledgement that providing effective consumer protection should involve paternalistic elements, a paternalistic approach constrains the freedom of contract and autonomy of the customer.[68] Although this paternalistic element has been acknowledged, the problematic question is to what extent this type of intervention should be implemented.[69] This degree of intervention interesting and when analysing the regulations will be discussed further, to explore ways to improve the current rules in place.

A factor which can contribute to vulnerability, is the age of the consumer.[70] A common issue that arose with regard to payday loans were the target audience of advertisements, these being vulnerable adults and children, of whom were being persuaded through quick and easy application processes.[71] The demand for high-cost short-term credit among young adults is worryingly high, further, a worrying number of undergraduate students have turned to high-cost short-term lenders, to cope with university expenses.[72] A great number of consumers had very low levels of financial understanding which led to them suffering from harm, specifically where lenders took advantage of their firms not being monitored and addressed properly.[73] At the height of the payday loan industry, lenders lent out money indiscriminately and where consumers could not repay, a short-term loan was offered to pay off one loan, resulting in one loan after another and then another.[74] Subsequently these vulnerable consumers were left drowning.[75]

[68] O'Shea, Fairweather, Grantham (n 55)
[69] ibid
[70] Fejos (n 1) 182
[71] ibid
[72] Aldohni (n 62) 324
[73] National Audit Office (n 17)
[74] James Moore, '*Payday lending isn't over yet- and now its victims are being shortchanged yet again*' (The Independent, 2019) >https://www.independent.co.uk/voices/wonga-loans-payday-lending-compensation-scheme-victims-wageday-a8852651.html <accessed 22 July 2019
[75] ibid

Mental health can be another factor which can contribute to a consumer being classified as financially vulnerable. Those consumers who suffer with mental health issues are at risk of debt, the charity 12 of Christians Against Poverty's debt advice found that mental health conditions were the primary driver for debt for one in every twelve of its clients.[76] People living with mental health conditions are susceptible to becoming victims of financial exclusion as they are more likely to be out of work or living an unstable lifestyle beyond their control.[77] Whilst a two-way relationship exists between mental health and financial exclusion, the experience of dealing with such a situation can have further negative effects such as stress, anxiety and depression, all of which can be attributed to their financial situation.[78]

Employment has also played a part in determining people who can fall within the financially vulnerable category. Payday loans have allowed consumers to mitigate financial distress in extraordinary or temporary circumstances and increase individual and community resilience to such financial downturns. [79] However, over the years, employment patterns have been subject to structural changes, this is due to a growth of both self and part-time employment, zero-hour contracts and cuts in state benefits, which have all brought about unpredictable incomes and led to the generation of financial instability.[80] The number of people who are self-employed has risen by 45% percent over the past years and more than nine-hundred thousand people are on zero-hour contracts, these have been referred to as the 'gig

[76] Financial Conduct Authority (n 58) 10
[77] House of Lords, Select Committee on Financial Exclusion, '*Tackling Financial Exclusion: A country that works for everyone?'* (Report of Session 2016-17) 51> https://publications.parliament.uk/pa/ld201617/ldselect/ldfinexcl/132/132.pdf <accessed 12 August 2019
[78] ibid
[79] Fejos (n 1) 188
[80] Consumer Finance Association, '*A Modern Credit Revolution: An Analysis of the Short-Term Credit Market'* (2017) < http://cfa-uk.co.uk/wp-content/uploads/2016/11/SMF-Report-AKT10796.pdf >accessed 03 August 2019

economy'.[81] Under both types of employment, there is no guaranteed or stable form of income.[82] A dip in income could lead to a serious and harmful result for the consumer, with many being unable to manage such a risk. These unpredictable circumstances mean that, in absence of savings, people may have to turn to credit to bridge the gap from a shortfall in income.[83]

Whilst consumers may always be classed as financially vulnerable, many consumers may experience vulnerability for just a short period of time, the most marginal debtors are payday loan consumers, whatever their household income may be.[84] Payday loan customers have a tendency to generate below average incomes, however, are not classified as poor.[85] The customers finances can be precarious, and in many cases are, however a payday lender offers to agree a cash advance to the consumer in exchange for up to the highest legal limit that can be charged as an interest rate.[86]

It is clear to see that many of the consumer protection issues involve people of a vulnerable nature, for example, people who are young and mentally ill, as well as those who have poor credit histories or who have experienced financial distress in the past. Whilst the FCA has recognised that limiting access to credit does not benefit the consumer in situations of temporary financial emergencies of a non-recurrent nature, it is clear that adversity has arisen due to a large number of agreements being entered into in the past.[87] Loans have

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[81] Jonathon Davidson, '*Getting affordability right in consumer credit*' (Speech, 2018) >https://www.fca.org.uk/news/speeches/getting-affordability-right-consumer-credit <accessed 22 August 2019
[82] Financial Conduct Authority, '*Alternatives to High-cost Credit Report*' (2019) 8 >https://www.fca.org.uk/publication/research/alternatives-high-cost-credit-report.pdf <accessed 22 August 2019
[83] ibid
[84] Robert Mayer, '*Quick Cash*' (Northern Illinois University Press, 2010) 145-146
[85] ibid
[86] ibid
[87] Smith (n 32) 15

particularly been made to consumers who have been unable to repay them on their given due date, which has resulted in the loan rolling over, increasing the cost of the repayment of the loan by a great amount. More often than not the loan would be rolled over more than once, this increase in the price of the loan, drastically increases the level of indebtedness which soon reaches an alarming level. [88]

Financial vulnerability comes in all shapes and sizes, and whilst many consumers may experience this financial vulnerability on a permanent basis, many experiences this for a short or temporary period of time as discussed. The problems that arise with this category being so broad is how to generate a set of criteria which would include all of these consumers under one roof. How can consumers be fully protected when this category of people does change on a regular basis? Should stronger protection be implemented for these consumers who are financially vulnerable, or does this simply limit access to credit for consumers as a whole?

Why is it important for consumers be able to access credit efficiently, and why access to credit should not be restricted?

Whilst great emphasis has been placed on the importance of protecting the consumer, it is just as important to discuss how access to credit must be balanced with this protection and how a complete ban on payday loans would not be the answer to solving the problems discussed above. It is apparent that consumer credit plays a vital role in everyday life for many consumers, it does so by providing flexibility in managing finances and allows goods and services to be available immediately, without the consumer having to wait and save to

[88] ibid

get them at a later date.[89] Contrary to many of the negative portrayal of the payday lending industry as being extortionate and unscrupulous, particularly by the media and campaigners, consumer credit borrowers have emphasised the positive aspects of being able to access payday loans, namely their ease of access and the ability to maintain dignity and privacy, as well as obtaining a level of responsibility and independence.[90]

Allowing consumers to access money immediately, or within a few hours, without the need to provide security, can provide a vital solution for consumers.[91] Therefore, the rise of the payday lending market filled a gap in the market and offered a solution to the demand for high cost short term credit. [92] A series of fundamental, yet interrelated, long term changes have occurred in the labour market in the UK which have led to a favourable climate for the increase in the number of payday loans granted.[93] However, it is important to see why access to credit is necessary and financial exclusion is not the best option when aiming to protect consumers. The term financial exclusion can be broad and henceforth can be used in various circumstances relating to lack of access to a range of financial services or a narrow concept reflecting different circumstances, for example exclusion due to charges and prices being prohibitively high.[94] Self-exclusion is also important, as this will permit a consumer from applying for such credit because they believe they will be refused, because of previous

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[89] Andrea Fejos, '*The Impact of Information on Responsible Lending and Responsible Borrowing in the European Union'* Journal of the Serbian Association of Lawyers 6(12) (2009) 751 > https://moodle.essex.ac.uk/pluginfile.php/704998/mod_resource/content/1/The%20Impact%20of%20Information%20on%20Responsible%20Lending%20and%20Borrowing%2C%20Andrea%20Fejos.pdf >accessed 22 May 2019

[90] Rowlingson, Appleyard, Gardner (n 23) 535

[91] Fejos (n 89) 751

[92] Aurora (n 1)

[93] Rowlingson, Appleyard, Gardner (n 23) 528

[94] Ramsay (n 48) 373

refusal or the belief that they do not accept people of the calibre they believe themselves to be.[95]

Economic development is key, and financial inclusion plays a vital part to this development. Research has demonstrated that financial inclusion matters for economic development and poverty reduction,[96] and this inclusion has said to reflect a growing realisation of its potentially transformative power to accelerate transformation gains.[97] Financial inclusion seeks to include the vulnerable sector of society in the formal banking system, to develop their financial wellbeing and to stimulate economic growth.[98] The primary goal of financial inclusion is concerned with members of society who have previously been excluded from formal banking, specifically concentrating on the extent and depth of a country's vulnerable sector engaging with its mainstream banking system.[99]

Whilst financial inclusion is important, a common argument for providing access to credit is that if rules and regulations make financial credit difficult to access, less people will be able to access the credit that they may need at a specific point in time.[100] This will disallow consumers from accessing products and services, potentially in exceptional circumstances when credit is needed immediately.[101] Further those who work in the consumer credit industry are likely to argue that limiting access to credit will force people in the direction of illegal loan sharks and generate greater issues for those who are unable to repay payday

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[95] ibid

[96] World Bank Group, '*Global Financial Development Report 2014: Financial Inclusion*' (2014) 5 > http://documents.worldbank.org/curated/en/225251468330270218/pdf/Global-financial-development-report-2014-financial-inclusion.pdf <accessed 22 August 2019

[97] ibid

[98] Jerry Buckland, '*Building Financial Resilience: Do Credit and Finance Schemes Serve or Impoverish Vulnerable People?*' (Pelgrave Macmillan, 2018) 19

[99] ibid

[100] Ramsay (n 48) 374

[101] Ramsay (n 48) 374

lenders.[102] If credit cannot be accessed in a safe and legal manner, consumers will seek for credit elsewhere, creating bigger problems for themselves, for example in Glasgow in the early 1980s illegal moneylending was found to be the most effective alternative where access to credit was not available.[103]

It is clear to see that access to financial services and financial inclusion are key issues which are fundamentally important to the functioning of the economy in the UK. Whilst the financially vulnerable sector has been focussed on here, it is important to note that financial inclusion matters to everybody, not just the disadvantaged or vulnerable.[104] Whilst intervention in the payday lending market to prevent borrowers from accessing credit inevitably undermines the rights of the borrowers, specifically their right to freely enter into contracts of their choice, it is still vital for consumer protection to be balanced with providing access to credit for consumers.[105]

The FCA's Responsible Lending Rules

The Creditworthiness Assessment and Affordability Assessment- Two Separate Tests

The primary focus throughout this research is being placed upon the responsible lending rules, introduced by the FCA, in response to severe criticism from consumers, debt charities and the governments recognition of such criticism. The introduction of these consumer protectionist measures aims to assess a consumer's creditworthiness and affordability, to ensure that the loan they wish to take out is practicable and affordable for both the consumer and the credit lender, whilst acting in a customer's best interests, and ensuring

[102] Carl Packman, '*Payday Lending: Global Growth of the High Cost Credit Market*' (1st edn, Pelgrave Macmillan, 2014) 118
[103] Ramsay (n 48) 374
[104] House of Commons Treasury Committee (n 63) 65
[105] Fairweather, O'Shea, Grantham (n 25) 132

the transparency of terms and conditions.[106] The FCA handbook provides two separate assessments of which firms must take into consideration before granting a loan to a consumer, thus being the risk of the credit and affordability of the loan.[107] The firm must undertake a creditworthiness assessment and have proper regard to the outcome of that assessment in respect of affordability risk.[108] These two tests are very different and should be assessed separately, as they both obtain important elements of consumer protection.[109] The credit risk primarily focuses on the risk to the lender that the consumer will not be able to meet the repayments, whilst the affordability risk focuses on how difficult the repayments may be for the consumer to repay the credit.[110] Differentiating between the two allows the credit risk to be a 'lender-focused' test, whilst the affordability risk acts as a 'borrower-focused' test.[111] A discussion of both assessments separately will portray the important role each play in protecting the consumer, and why they have been introduced as separate tests will demonstrate the FCA's push towards a stronger, more efficient protection of consumers from these harmful credit lenders. The regulation and guidance will be analysed to portray any flaws they possess, and further, it will seek to determine whether these regulations and guidance are strong enough to protect the financially vulnerable. Further, it will determine whether stronger protection is needed, or the government needs to support or implement better alternatives.

<u>Creditworthiness Assessment</u>

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[106] Financial Conduct Authority, 'Assessing creditworthiness in consumer credit- Feedback on CP17/27 and final rules and guidance' (PS18/19, 2018) 11 > https://www.fca.org.uk/publication/policy/ps18-19.pdf <accessed 22 August 2019
[107] Consumer Credit Sourcebook CONC 5.2A.10 R
[108] Consumer Credit Sourcebook CONC 5.2A.5
[109] FCA, '*Assessing Creditworthiness in Consumer Credit'* Consultation Paper CP17/27 (2017) 4 >https://www.fca.org.uk/publication/consultation/cp17-27.pdf <accessed 26 May 2019
[110] ibid
[111] ibid

The first of the responsible lending rules to be analysed will be the creditworthiness assessment, as this was one of the first rules to be implemented by the FCA. Its introduction as a responsible lending rule formed a starting point for rules and guidance to be put in place to contribute towards protecting consumers from harmful practices, for example the FCA provides that a credit lender must undertake a reasonable assessment of the creditworthiness of a customer before entering into a regulated credit agreement, or significantly increasing the amount of credit provided.[112] A firm must base its creditworthiness assessment on sufficient information: of which it is aware at the time the creditworthiness assessment is carried out; obtained where appropriate, from the customer, and where necessary from a credit reference agency and the information must enable the firm to carry out a reasonable creditworthiness assessment.[113] Whilst this is a starting point for the FCA, discrepancies and flaws in this rule are immediately apparent.

One would argue that the first issue that arises with this rather small section of the regulation is that there is an underlying uncertainty as to what firms should regard as a 'significant increase'. The FCA made it clear that it did not want to be overly prescriptive as to when an increase should be deemed significant.[114] However, they also made it clear that they did wish to clarify that multiple separate increases, which may be seen as insignificantly individually, could result in a significant increase, resulting in the need for a further creditworthiness assessment.[115]

It is clear to see that the problem here is that what may be deemed to be a significant increase to one firm, may not be deemed the same by another. One would argue that the

[112] Consumer Credit Sourcebook CONC 5.2A.4(1)(2)
[113] Consumer Credit Sourcebook CONC 5.2A.7
[114] Financial Conduct Authority (n 106) 11
[115] ibid

FCA emphasised that separate increases may be regarded as a significant increase, to provide flexibility for credit lenders and stay away from restrictive measures which could potentially jeopardise access to credit. Whilst this does provide a level of scope and flexibility for firms to develop their own tests, it also provides scope for firms to increase a consumer's credit limit by a significant amount and simply say that it was regarded as insignificant. This argument stems from the issues that consumer credit firms have raised, namely the issue they have with the uncertainty that it causes, with many having sought further clarification on this term.[116] A number of firms believe that guidance on what would constitute a significant increase would be of great use to them, with some consumer groups arguing that assessments should be required for any credit limit increase.[117] One would argue that whilst requiring a creditworthiness assessment for every credit limit increase would be burdensome to credit lenders, increasing their workload, potentially decreasing profits, to fully protect consumers, this level of protection is needed, particularly for the financially vulnerable.

Referring back to the paternalistic elements discussed earlier, one would say that a level of paternalism is needed here. If individuals are struggling financially, many would go to far lengths to get the credit they need, particularly as the upsurge in the use of high-cost credit was to 'make ends meet'.[118] With the history being particularly bad in this area, credit should not be increased unless another creditworthiness assessment is carried out. This avoids any potential prediction of missed payments and ensures that a credit lender does not allow someone, who is finically vulnerable, to enter into a spiralling debt that the lender

[116] ibid
[117] ibid
[118] Fairweather, O'Shea, Grantham (n 25) 136

can potentially foresee. The initial basis for these regulations is to protect consumers from unscrupulous practices such as increases credit limits without checking the consumers creditworthiness, henceforth why should there be scope for credit lenders to abuse such regulations. Merely providing that a creditworthiness assessment is required only for significant increases, does not address the fact that consumers have taken out credit based on their creditworthiness at the time of the initial assessment, why should their credit limit be increased when their initial creditworthiness assessment had already set the bar of their credit limit? Increasing the credit limit without a creditworthiness assessment is merely an attractive feature for credit lenders to use to gain custom and allow consumers to fall into spiralling debt traps. It is imperative that one thinks back to why these regulations were implemented in the first place. It is apparent here that the FCA has tried to balance consumer protection with access to credit, however the access to credit element has tipped the scales, leaving consumers to be subject to the terms of the credit lender and open to harm. Further, evidence shows that credit lenders are confused as to what should be deemed as significant, their call for further guidance merely demonstrates that lenders are unsure, if lenders are unsure, how can the FCA be sure that consumers are getting the level of protection that they deserve?

A further requirement in the creditworthiness assessment, is that to aid in assessing the financial standing of consumers and allow them to gain access to a range of financial services is the credit information of the consumer, which can be provided by a CRA.[119] A CRA collects and records either public information or credit account information on a person's

[119] Financial Conduct Authority, *'Credit Information Market Study: Terms of Reference'* MS19/1.1 (2019) 3 > https://www.fca.org.uk/publication/market-studies/ms19-1-1.pdf <accessed 30 July 2019

creditworthiness, which can then be given to lenders and credit providers.[120] However, it is important to note that the CRA's do not determine whether the loan should be granted or not, therefore one lender may decide to grant the loan, when another may not.[121] The information provided by CRA's is important and helps to move towards financial lenders acting and lending in a responsible manner.[122]

However, it can be argued that using CRA's can be problematic from a consumer protection perspective. Although the CRA's do not make the decision for the credit lender, it is interesting to explore how efficient these agencies are, and whether the information they provide should be used by credit lenders to make the decision on whether or not to lend to a consumer. Concerns have been raised about the coverage and quality of credit information provided, the effectiveness of competition between CRA, and the extent of consumer engagement.[123] A crucial aspect is that not all credit lenders report data to more than one CRA, therefore the reliance on the information provided by CRA's has contributed to the downfall of the implementation of the FCA consumer credit rules as well as consumer protection.[124]

Further and rather a major criticism of the FCA is that at this time they will not consult on real time data sharing requirements.[125] Lenders providing data to CRA's on a regular basis, typically a minimum of once a month, is one of the reciprocal principles that underpin data sharing.[126] However, even when the data is provided this regularly, it can be as old as sixty

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[120] Tony Boczko, '*Managing Your Money: A Practical Guide to Personal Finance*' (Palgrave Macmillan, 2016) 66
[121] Timothy Edmonds, '*Credit Reference Agencies*' (House of Commons Briefing Paper, 2014) 5 > https://researchbriefings.files.parliament.uk/documents/SN04070/SN04070.pdf <accessed 12 August 2019
[122] Financial Conduct Authority (n 119) 3
[123] ibid
[124] House of Commons, '*Real-time Credit Scoring*' (2016) 605 > https://hansard.parliament.uk/Commons/2016-02-02/debates/16020280000003/Real-TimeCreditScoring <accessed 12 August 2019
[125] ibid
[126] ibid

days before it is made available to other lenders.[127] This can have a negative effect on competition creating serious consequences, however, is it particularly problematic for consumer welfare.[128] Credit lenders not being able to access the most recent sixty days of the consumers credit history can result in loans being given to consumers who cannot afford to repay, subsequently resulting in unaffordable levels of debt for the consumer. This problematic not only for consumer protection as a whole, it also would benefit the financially vulnerable consumer. It would allow firms to better identify a consumers financial position, for example having a clearer picture of a consumers credit history, whether it be their lack of one due to age, one particular vulnerability, or recent missed payments which could be the very start of a poor credit history, again a vulnerable criterion which has been identified as a factor of financial vulnerability. Further, the question as to which lenders share information is an entirely commercial decision, and it is left up to the credit lenders to assess whether it is in their interests to grant the loan, they do not have to take into account any other information, such as the wider benefits to consumers.[129]

A survey carried out by the FCA found that 96% of the firms who took part in their survey used CRA's.[130] For such a large number of firms to be turning to these agencies, surely the FCA should consider addressing the discrepancies they cause, and the potential these discrepancies have to jeopardise protection for, particularly for the financially vulnerable consumers. Data sharing could be an improvement for consumer protection and a possible recommendation for the FCA to research further. The absence of real-time data sharing is important for two key reasons, firstly because It is said to attribute to the cause of

[127] ibid
[128] ibid
[129] ibid
[130] Financial Conduct Authority (n 114) 21

unaffordable personal debt, arguably consumers are granted loans which are not truly affordable to them due to the fact that providers lack up to date records regarding their most recent liabilities and missed payments.[131] Secondly, it has been said to limit the effectiveness of competition in many overlapping markets, as it deters providers from entering the market and limits their ability to compete on a fair basis.[132]

One would argue that the FCA would benefit from revising the proposed strategy and develop regulatory solutions that encourage real-time data sharing and allows the innovative use of new technology.[133] If the CRA's data is not up to date, then assessments carried out by lenders are unlikely to accurately reflect the credit risk, or risk of financial distress at the time lenders are assessing the applications.[134] Having access to out of date credit information means that it is impossible for credit lenders to conduct an accurate assessment of the consumers credit history, generating several adverse effects including loans made to consumers who cannot afford to repay, worsening their already bad financial position. These debts further increase bad debt for the credit lenders who as a result raise their interest rates to cover such losses. These higher interest rates have a knock-on effect for the consumers as it makes the loan more difficult to pay, resulting in an escalating spiral of high interest rates and consumer debt traps.[135] Further, going back to the issues caused by increasing the loan without another creditworthiness assessment, if the CRA's data is months behind, the consumer may have taken out another loan during this period of time

[131] House of Commons (n 123) 605
[132] ibid
[133] ibid
[134] Financial Conduct Authority (n 11) 9
[135] Simon Grossman, *'Evidence to the Business, Innovation & Skills Committee on real-time data sharing submitted on behalf of 118 118 Money'* (2013) 1 > https://www.parliament.uk/documents/commons-committees/business-innovation-and-skills/118118-Money.pdf <accessed 12 August 2019

and substantially the lender is increasing a loan without having any knowledge of such financial affairs.

A further criteria included in the creditworthiness assessment regulation is that the credit lender must consider the risk that the customers will not make the repayments under the agreement by their due dates, and the risk to the customer of not being able to make repayments under the agreement in accordance with the affordability risk.[136] The guidance provided alongside this responsible lending rule provides that in relation to this rule, there may be circumstances in which the risk that one repayment will be missed or will be late is relevant to the creditworthiness assessment.[137]

Questions are immediately raised when reading this guidance, a question of particular importance is, whether this rule is strict enough? Whilst the firms must consider the risk of non-repayment, there 'may' be circumstances where the risk of missing one repayment could be relevant to the firm's assessment. In a consultation paper composed by the FCA, it was stated that whilst they wanted to avoid being too prescriptive, due to the fact that this could have harmful unintended consequences, they still wanted firms to be proportionate in their approach, and take into consideration the costs and risks of the credit for the individual consumer, as well as the probability that they may suffer harm as a result of the credit.[138] This is another clear example of the FCA attempting to balance consumer protection with access to credit. Flexibility can be seen throughout the regulations, for example in the first rule discussed there were problems with the terminology, which the FCA did not want to clarify further due to the level of flexibility they wanted to maintain.

[136] Consumer Credit Sourcebook CONC 5.2A.10
[137] Consumer Credit Sourcebook CONC 5.2A.11
[138] Financial Conduct Authority (n 109) 5

However, one would argue that the issue here is that if a company offering credit can foresee that the customer will miss a payment the practicable response is that the consumer should not be given the credit. Further, if one missed repayment can be foreseen, how can a firm truly show that they only foresaw one repayment? How can the consumer catch up with this repayment? So many questions arising merely from this small section of guidance, which one would suggest that the FCA needs to think more clearly about.

Whilst the FCA has introduced this section into the responsible lending rules, like many sections this is merely guidance and not a set rule. It is clear to see that by strictly keeping this as guidance for credit lenders and not enforcing it as a regulation, gives firms the ability to generate their own creditworthiness assessment and the flexibility provided to allow access to credit. However, the rule is flexible enough for firms to disregard whether consumers can make repayments, and even where repayments are foreseen to be missed, the loan can still be granted to the consumer. Research carried out by the FCA found that consumers appear to have a higher risk of a bad credit 'event', such as missing a loan payment, in the three to twelve months after taking out a payday loan than would have been expected, taking into account their credit history.[139] The question here is, what does this mean for a financially vulnerable consumer? One would argue that it simply means that those who are subject to vulnerabilities can fall through the loopholes provided here. Someone who can be foreseen to miss a payment can still be granted a loan. Young people who are new to the credit industry, or people who lack the capacity to understand the credit industry, or simply people who are uneducated with regards to handling finances, these people could be easily led to believe that it is okay to miss a payment. If the credit lender

[139] Financial Conduct Authority, *'High-Cost Credit: Including review of the high-cost short-term credit price cap'* (FS17/2, 2017) 12 > https://www.fca.org.uk/publication/feedback/fs17-02.pdf <accessed 22 August 2019

can foresee a missed payment, and the consumer can also foresee that they will miss a payment, but the loan is needed so badly the consumer disregards their affordability, it can lead to consumer believing that they can miss a repayment and everything will be okay. Further consumers who are vulnerable due to their employment, be in zero-hours contract or self-employed, a credit lender may foresee that consumer will miss a payment due to their employment status. However, if they can foresee one missed payment, who can say they will not miss any further payments. These fluctuating employment patterns could subject the consumer to a loan where only one missed payment is foreseen by the credit lender when in fact the work may simply not be there the next month, or the month after that, the consumer is then left with a high-interest loan they cannot afford to repay.

Although this argument is easier to see from a consumer protection perspective, when trying to balance this with providing access to credit, further issues arise. To give an example, if this guidance was to be made a rule, a stricter approach would restrict firms from providing credit and disallow consumers who may fall into the scope from gaining access to credit, generating a knock on effect of which denying access to credit results in, as discussed earlier. It is clear to see that it is very hard to strike the perfect balance between consumer protection and providing access to credit, however to protect these financially vulnerable consumers from unscrupulous practices, and the harm that has been so evident in the past, these firmer measures need to be implemented. One would question as to why this guidance has been introduced when there is so much scope for firms to completely disregard it? Surely this is not providing an adequate answer to the problems discussed earlier in relation to unscrupulous practices and the neglection of consumer protection.

Throughout the creditworthiness assessment, the FCA requires firms to maintain a level of proportionality, the FCA provides that the information provided must be appropriate and proportionate to obtain and assess.[140] When assessing a consumer's creditworthiness for the loan, the responsible lending rules require the credit lender to demonstrate a degree of proportionality when making its judgement on whether or not to grant a loan.[141] The extent and scope of the creditworthiness assessment, and the steps that the firm must take to satisfy the requirement that the assessment is a reasonable one, based on sufficient information, are dependent upon, and proportionate to, the individual circumstances of each case.[142] The term proportionality is used by the FCA numerous times throughout the creditworthiness assessment and again emphasises that the current rules imposed by the FCA gives credit lenders the flexibility to make reasonable assessments, based on the facts of the case at hand, demonstrating once again a strong focus on balancing access to credit with consumer protection.

However, if challenged by the FCA, the credit lender must demonstrate the basis on which they made their decision, adhering the proportionality requirement, justifying this level of flexibility as they believe that being unduly prescriptive could result in firms unnecessarily limiting lending and excluding customers who could afford to repay.[143] Further, it could slow down the credit lending process, meaning that it would take consumers longer to be granted credit which is said to likely to result in consumers switching firms, or even turning to other, less appropriate forms of credit, such as loans with lower instalments yet a higher

[140] CONC 5.2A.8
[141] CONC 5.2A.15 (1)(a)
[142] CONC 5.2A.20(1)
[143] Financial Conduct Authority, *'Assessing creditworthiness in consumer credit Proposed changes to our rules and guidance'* (CP17/27, 2017) 18 >https://www.fca.org.uk/publication/consultation/cp17-27.pdf <accessed 19 August 2019

overall cost.[144] The FCA have acknowledged that concerns have been raised by both credit lenders and consumers regarding the guidance and detail on what firms should consider whilst making a creditworthiness assessment, with the desire for better guidance on this. What should firms deem to be reasonable? What one may deem to be reasonable another may not, one would question whether there should be a threshold, or something more than simply saying it should be reasonable. Further, they have emphasised that their approach is designed to allow firms to create their own processes having regard to proportionality.[145] Here similar issues are raised to those discussed with regard to the guidance provided by the FCA, the scope that the guidance provides, likewise with proportionality, merely jeopardises the effectiveness of the consumer protection regulations.

Affordability assessment

The second half of the responsible lending assessment focuses on the consumers affordability. It has been clear to see that the absence of adequate affordability rules can result in consumers suffering from potentially avoidable financial distress.[146] Therefore the FCA introduced an affordability assessment which provides that a credit lender must consider the customer's ability to make repayments under the agreement, out of or using: the customers income, income from savings or assets jointly held by the customer with another person, without the customer having to borrow to meet the repayments, without failing to make any other payment the customers has a contractual or statutory obligation

[144] ibid
[145] ibid
[146] Financial Conduct Authority (n 11) 3

to make and without the repayments having a significant adverse impact on the customers financial situation.[147]

Ensuring that a customer can repay the loan without it having an adverse impact on the customers financial situation, one would argue is a great step towards ensuring the consumer is protected from taking out a burdensome loan that they will struggle to repay, creating a safety net for consumers. Although this regulation in place, the FCA has allowed scope for the credit lender by providing that this rule applies unless the firm can demonstrate that it is obvious in the circumstances of the particular case that the customer is able to make repayments in accordance with this rule.[148] Prior to these regulations being enforced by the FCA credit lenders raised concerns that greater emphasis on affordability may deter consumers from applying for a loan because the affordability requirements could become disproportionate to the credit obligation they were considering.[149] The credit lenders expressed dismay emphasising that such requirements would be inappropriate and risk significantly increasing costs and reducing the availability of credit.[150] Consumer organisations were concerned about this level of discretion and felt that restrictions should be placed upon it, further, many argued that income and expenditure should be assessed in all circumstances.[151]

One would say that it is apparent to see that the FCA has tried here to include a flexible approach to the affordability test by incorporating such rules, however it also demonstrates

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[147] Consumer Credit Sourcebook CONC 5.2A.12
[148] Consumer Credit Sourcebook CONC 5.2A.15(1)(a)
[149] Financial Conduct Authority, '*Assessing Creditworthiness in Consumer Credit: Summary of Research Findings*' (2017) 60 >https://www.fca.org.uk/publication/consultation/cp17-27-research-findings.pdf <accessed 02 August 2019
[150] ibid
[151] Financial Conduct Authority, '*Assessing creditworthiness in consumer credit'* (PS18/19, 2018) 14 > https://www.fca.org.uk/publication/policy/ps18-19.pdf <accessed 22 August 2019

a slightly relaxed approach to the regulation. It is practicable to argue that it is pointless for firms to carry out an affordability assessment when they are provided with the scope to simply say it was 'obvious' from the circumstances that the consumer could afford the loan. One would argue that this approach is very hard to enforce and fails to consider what criterions should be factored into this approach. If anything, one would argue that this is an easy way out for firms who fail to carry out adequate affordability assessments, further what may be obvious to one person, may be as unobvious to another. Whilst it is clear that this regulation would be determined on the merits of each case, who has the right to say that the circumstances of the case make it obvious that the consumer can repay the loan? Taking out a loan should be based on hard facts rather than a credit lenders opinion of a situation. Again, this raises red flags as far as the financially vulnerable are concerned, it leaves them wide open for credit lenders to take advantage of whatever vulnerability they may possess. The FCA have identified this issue and stated that whilst feedback from firms and their supervisory experience suggest there is still some uncertainty about regulatory expectations, in particular how far firms are expected to go with regard to assessing affordability and what procedures should underpin this, they particularly highlighted that whilst some firms may not be doing enough, others may be doing more than is required or necessary in the circumstances.[152]

For the purpose of considering the customer's income, under the affordability assessment, the FCA requires that it is not generally sufficient to rely solely on a statement of current income made by the customer without independent evidence, for example, in the form of information supplied by a CRA or documentation of a third party supplied by the third party

[152] Financial Conduct Authority (n 143) 20

or by the customer.[153] However, once again this is guidance as opposed to a regulation, the use of the phrase 'is not generally sufficient' emphasises the firms free reign to decide upon how they carry out their affordability assessment. Further, the use of this abstract term of phrase makes the regulation very confusing. On the one hand firms are being told to take into account the customers income, to ensure that the loan repayments do not have a significant adverse impact on the customers financial situation, whereas on the other hand they are being told that it is not generally sufficient to rely on a statement by the consumer. How are firms meant to interpret this? One would interpret this as whilst solely accepting a customer's statement is frowned upon, there is scope to solely accept this without any negative repercussions. There is scope for lenders to do more to obtain proof and undertake a more thorough assessment of borrowers' potential vulnerability.[154] This is a clear indication that the FCA responsible lending rules need to be stronger to ensure that firms routinely carry out rigorous affordability checks.[155]

When the Office of Fair Trading carried out an assessment, they reported that they had found that whilst 74% of lenders carry out an affordability assessment for all new customers, 67% said they did so for every new loan, and only a mere 23% did so for each loan rollover.[156] These statistics are very interesting, it is apparent that only 26% of all of the lenders who took part in the questionnaire do not even carry out an affordability assessment for new customers.[157]Whilst analysing each section, and highlighting key words that create these grey areas, research has found that different lenders take very different

[153] Consumer Credit Sourcebook CONC 5.2A.16(3)
[154] Citizens Advice (n 7) 14
[155] ibid
[156] Office of Fair Trading, '*Payday Lending: Compliance Review Final Report*' (2013) 12 > https://assets.publishing.service.gov.uk/media/532ad55eed915d0e5d00038d/oft1481.pdf <accessed 30 July 2019
[157] ibid

approaches when making these assessments. Whilst again this creates the flexibility for firms to allow consumers to access credit, serious concerns have been raised with regard to lenders gathering a sufficient amount of information to make a reliable affordability assessment, or to properly check the information they do receive.[158] Initially one would have argued that the introduction of an affordability assessment was a step forward in ensuring consumers are fully protected. However, its effectiveness would allow one to argue otherwise. The initial idea has lost its practicality due to the gaps in the regulation which allow it to be subject to abuse, jeopardising consumer protection and subsequently not doing what it set out to do.

When discussing the affordability assessment, a former credit lender that is particularly interesting to look at is Wonga, a lender who entered administration in 2018, the key issue in this firm's collapse being affordability.[159] Whilst Wonga received complaints regarding the affordability of their loans prior to the FCA introducing the affordability assessment in 2014, many complaints were also received after the FCA introduced this requirement.[160] Evidence demonstrated that loans even up until 2017 loans were made without adequate affordability checks being made.[161] Wonga's payday loans have been referred to as 'the crack cocaine of debt, unneeded, unwanted, unhelpful, destructive and addictive'.[162] However, whilst many have been glad to see Wonga gone, not all payday lenders are

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[158] Ibid 10
[159] Jonathan Davidson, Executive Director of Supervision – Retail and Authorisations, at the Credit Summit, London (2019) > https://www.fca.org.uk/news/speeches/what-can-consumer-credit-sector-expect-from-fca <accessed 30 July 2019
[160] Damon Gibbons, *'The Collapse of Wonga: Government must act to secure justice for consumers but there are wider lessons to be learnt'* (Centre for responsible credit, 2018) 4 >https://www.responsible-credit.org.uk/wp-content/uploads/2018/09/The-collapse-of-Wonga.pdf <accessed 30 July 2019
[161] ibis
[162] Sean Feast, '*Why we should care about Wonga's demise*' (Institute of Credit Management, 2018) 4 > http://content.ebscohost.com/ContentServer.asp?EbscoContent=dGJyMNLe80SeprY4v%2BvlOLCmr1Gep7VSrqi4SbaWxWXS&ContentCustomer=dGJyMPGvtkmyqLdNuePfgeyx9Yvf5ucA&T=P&P=AN&S=R&D=bsu&K=132157816 <accessed 08 August 2019

inherently evil and whilst companies like Wonga have crumbled, providing alternative methods of lending have been alarmingly slow.[163] The collapse of Wonga raised fundamental questions about the FCA's regulations and guidance, particularly concerning the affordability assessment.[164] Whilst the FCA has consistently stood its ground on fettering a credit lenders discretion to decide what is and what is not affordable, their reluctance to interfere and impose a clear judgement regarding affordability means that lenders will always seek what is in the firm's best interest.[165] It is easy to argue that for as long as the FCA continue to do this, the affordability assessment will always provide gaps in the so called safety net which vulnerable consumers are highly likely to fall through. Research found that whilst affordability and culture identified much improved compliance for many firms, the firms that were doing best were those that went above and beyond a compliance culture and purposefully fixated their culture on customer outcomes.[166] However, Wonga is a clear example of a firm who failed to do this, and again one would question whether firms should have to purposefully fixate their culture on customer outcomes? Should regulation be put in place which already fixates customer outcomes for them?

Poor affordability assessments have been recognised despite the introduction of an affordability assessment. One main issue that was recognised was the verification of whether credit lenders are carrying out sufficient affordability assessments, this is significantly difficult to do. Not do the rules provide too much scope for lenders to abuse them, the scope makes it difficult for the rules to be enforced. Further, the expense of carrying out such an assessment as well as the time it takes to do so is merely a burden on

[163] ibid
[164] Gibbons (n 160) 4
[165] ibid
[166] Davidson (n 159)

the lender certainly not in their best interests as far as business is concerned.[167] ‘It is all well and good having a range of new regulations and expectations of an industry that is famed across the western world for its relaxed attitude to sticking with guidance, this counts for nothing if enforcement of law shares this relaxed approach’.[168] This overall summation given by independent researcher Carl Packman perfectly sums up the current regulations in the UK. The relaxed approach to the guidance provided by the FCA allows these financially vulnerable sector to slip through the safety net that this guidance should be providing, and if firms can get away with the bare minimum where consumer protection is concerned, the FCA’s regulations and guidance are seemingly worthless.

<u>Summary of responsible lending rules</u>

In summary, it is clear to see that both aspects of the responsible lending rules have issues with providing effective consumer protection. A report carried out by the National Audit Office found that regulation of the consumer credit market does provide benefits to consumers, however the regulatory regime is not fully effective as it does not fully minimise harm from unscrupulous trading practices. [169] If one were to summarise the effectiveness of the responsible lending rules, it is clear to see that whilst regulation has led to much better protection for consumers, there is far too much scope for the rules to be fully effective.

A review by the FCA demonstrates that the introduction of the responsible lending rules has provided substantial benefits for consumers.[170] The review found that 760,000 borrowers in the payday lending market are saving a total of £150m per year, credit firms unlikely to lend

[167] Packman (n 102) 127
[168] Ibid 76
[169] National Audit Office (n 17)
[170] Financial Conduct Authority, ‘Financial Conduct Authority sets out agenda and priorities for consumer credit’ (2017) >https://www.fca.org.uk/news/press-releases/agenda-priorities-consumer-credit <accessed 06 August 2019

to customers who cannot afford to repay the loan, and debt charities such as Stepchange, are seeing far fewer clients with debt problems linked to high-cost short-term credit.[171] Whilst the consumer protection has provided benefits, it is hard to ignore the discrepancies, alongside the uncertainty that come with the responsible lending rules, which have led cracks forming and vulnerable consumers being subjected to falling through these cracks. The dominant portrayal of payday lending led to the introduction of the responsible lending rules by the FCA, and tightened regulation on consumer credit lenders, following the changes, the number of loans and the amount borrowed from payday lenders dropped by 35%.[172] Despite this drop, many campaigners argued for further regulation to better strengthen consumer protection.[173] With the current measures in place campaigners argued that people who are of a financially vulnerable nature would be better off without access to payday lending.[174] In a press release, the chief executive of the FCA stated that high cost credit products remain a key focus for the FCA due to the risks that they pose for the vulnerable consumer.[175] He also emphasised that the FCA were pleased with the marked improvement in the payday loan sector following on from a period where lenders treated the customers in an unacceptable manner.[176] However, once again it must be emphasised how important access to credit is, and how tightening consumer protection is essentially going to ruin the payday lending market. If rules are too strict and do not provide a good degree of flexibility for firms, it is likely that credit lenders will turn away from the payday loan market and assert their business elsewhere, limiting access to credit. Further if rules

[171] ibid
[172] Rowlingson, Appleyard, Gardener (n 23) 539
[173] ibid
[174] ibid
[175] Financial Conduct Authority (n 170)
[176] ibid

are too strict, consumers will not be able to access credit, again jeopardising the payday loan market and restricting access to credit.

When so many people are relying on payday loans, it is practicable to argue that consumer protection should be tightened, however balancing this with access to credit is rather difficult to do. If consumers cannot be fully protected and access to credit balanced alongside this consumer protection, which has been seen to be a recurring issue throughout this research, surely the FCA and the government should be looking at ways to provide alternatives to payday lending and prevent the financially vulnerable from being excluded from accessing credit, which is apparently essential in many households.

Alternatives to Payday Lending

Credit Unions

As an alternative method of accessing credit, an interesting area to explore is that of Credit Unions. These are not for profit credit unions who offer financial services to almost one million people in the UK.[177] It is important to explore the importance of credit unions, as it is arguable that their structure and use as international alternatives to accessing affordable credit, could be used as baseline structure for a government implemented scheme in the UK. Whilst vulnerable consumers may find it difficult to manage any unexpected expense, in everyday life it is very likely that this type of consumer may have to borrow money to meet these unexpected financial needs.[178] Although financially vulnerable consumers may find

[177] Carmichael (n 53)
[178] StepChange, 'What sort of credit can help low income households: A segmentation of the need for affordable credit' (2018) 5 > https://www.stepchange.org/Portals/0/documents/Reports/stepchange-debt-charity-affordable-credit-march-2018.pdf <accessed 08 August 2019

themselves excluded from mainstream credit, they may still meet the requirements of the creditworthiness assessments for credit union loans.[179]

Credit unions conduct their business for members through a financial co-operative, with the key purpose of receiving from and to make loans to members. Although they do not serve the general public, membership can be gained through meeting the qualification criteria.[180] Under the rules of the society admission to membership must be restricted to persons who fall within one or more common bonds appropriate to a credit union,[181] some examples of these common bonds are: following a particular occupation, being employed by a particular employer or residing or being employed in a particular locality, to name just a few.[182] Whilst the main purpose of these unions is to provide loans, generally the law limits its loan terms to ensure that the loans granted are of maximum benefit to the consumer, however balances the protection of the credit unions interests.[183]

An important point to consider is that the stark contrast between payday lending and credit unions is that the credit unions offer fair and reasonable fees, London Mutual Credit Union for example advance a loan of one hundred pounds for one month at just a cost of three pounds, therefore the borrower only has to pay one hundred and three pounds on the next payday.[184] Whilst this type of loan seems to be a much better alternative to payday lending,

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[179] ibid
[180] Nicholas Ryder, '*Credit Union Legislative Frameworks in the United States of America and the United Kingdon- A Flexible Friend or a Step Towards the Dark Side?*' J Consum Policy 31 (2008) 147 >http://content.ebscohost.com/ContentServer.asp?EbscoContent=dGJyMMTo50SeqLQ4yOvqOLCmr1GeprVSsKi4S7eWxWXS&ContentCustomer=dGJyMPGvtkmyqLdNuePfgeyx9Yvf5ucA&T=P&P=AN&S=R&D=bsu&K=31893376 <accessed 26 July 2019
[181] Credit Unions Act (1979) S1A(1)
[182] Credit Unions Act (1979) S1A (2)(a)(b)(c)
[183] Ryder (n 180) 155
[184] Carmichael (n 53)

there are prominent issues with credit unions which result in consumers not taking out loans with them.

Although this category of consumers may be eligible for this type of lending, there are still barriers which subject the financially vulnerable to exclusion. The greater availability and awareness of this affordable credit provision is an issue, there is a low awareness of credit unions and their purposes which mean these consumers will not access such credit due to them simply being unaware that this form of lending may be available to them.[185] Further, credit unions are very different from commercial lenders as they do not have the same level of expenditure to invest in advertising to make people aware of their services.[186] Also as discussed earlier, one of the common bonds is to reside in the area of the credit union the consumer wishes to take a loan from, however geographical or practical barriers arise when consumers try to access these lenders when they're not available in their local area.[187] A further issue is that whilst the interest charged by credit unions loans is capped at 3%, offering credit up to this interest per month may not allow credit unions to provide loans for higher risk consumers. Whilst the appeal of these low interest loans may be great for many consumers, higher risk consumers are still likely to be subjected to financial exclusion. However, increasing the 3% cap on interest is unlikely to solve this issue as credit unions are unlikely to want to lend credit to higher risk consumers.[188]

It is clear to see that credit unions have their pros and cons, providing a loan which has a maximum benefit to the consumer whilst balancing the credit unions interests is a clear example of how the consumer is put first and not how much profit a firm can make from the

[185] StepChange (n 178) 5
[186] ibid
[187] ibid
[188] Financial Conduct Authority (n 82) 10

consumers repayments. One would state that credit unions provide a good base layer for a government implemented loan scheme, they provide loans to people who may not be eligible for mainstream credit, their interest rates are substantially lower than payday lenders and they provide affordable loans for those who may slip between the consumer protection regulations provided by the FCA for the payday loan market. Whilst the government would have a long way to go to implement or support such a scheme, and these criterions alone would not be sufficient to create such, one would argue that these basic ingredients used by credit unions to offer loans would be a great starting point for a government implemented scheme, focussed towards the financially vulnerable.

The FCA have acknowledged the benefits credit unions can bring as an alternative to payday lending, however, have also acknowledged the issues currently standing with credit unions.[189] A report has shown that the FCA want to see credit unions maximise their potential for growth with the help of the HM Treasury to consider in the longer term whether there is value in reviewing credit union legislating and facilitate the growth of larger credit unions.[190] Further they would like to see credit union representatives working together to speak up with a more unified voice, making credit unions better known to consumers and aiding in their growth.[191] If people were made aware of these alternatives, arguably consumer protection provided by the responsible lending rules would not have to be strengthened as there would be alternatives for the financially vulnerable to turn to. It is apparent that the FCA needs to do something more to protect the financially vulnerable, be it improve the level of consumer protection provided by the responsible lending rules or

[189] ibid
[190] ibid
[191] ibid

simply to help aid the growth of credit unions, allowing the financially vulnerable to identify that there are other means of taking out a loan, where the loan is genuinely in the best interest of the consumer and not a hard headed credit lender who is focussing on making a profit.

Budgeting Loans

Another alternative, offered by the government, are budgeting loans. The government has identified the issues with payday lending and has to an extent taken action by providing an alternative to high cost short term credit, as demonstrated through the introduction of budgeting loans. Budgeting loans were introduced with the intention of defraying irregular expenses, allowing access to affordable credit for lump-sum expenses.[192] Budgeting loans can be given for an array of expenses, including essential household items, rent in advance, repaying hire purchase loans or repaying loans for items such as furniture or household items.[193] These loans are repaid in the form of an interest free loan which is paid back to the government from weekly benefit deductions[194]. Whilst the maximum loan that can be granted is £1000, and the minimum being £30, these loans were only introduced for people on income related benefits, providing them with an alternative and preventing them from being forced to rely upon unscrupulous and extortionate lenders.[195] These loans are only available to people who have been on income support or income based jobseekers

[192] Select Committee on Social Security, *'Memorandum submitted by the Department of Social Security'* (Minutes of evidence, 2001) >https://publications.parliament.uk/pa/cm200001/cmselect/cmsocsec/232/1030702.htm< accessed 09 August 2019
[193] GOV.UK, *'Budgeting Loans'* >https://www.gov.uk/budgeting-help-benefits <accessed 28 August 2019
[194] Select Committee on Social Security (n 192)
[195] ibid

allowance for at least twenty-six weeks.[196] This means that people who are not eligible for benefits cannot be eligible for such a loan.

Once again, immediate flaws cannot be highlighted when offering these loans. Whilst one would state that this is good idea and a step forward by the government, the responsible lending rules focus on a consumer's income, various types of people can be subject to financial vulnerabilities, not strictly those who receive benefits. For example, self-employed people or those on zero-hour contracts, they would not be able to access these loans even when they really need them, as their income is not provided by the government through a benefits scheme. The criteria for budgeting loans is unfair, people who work and cannot claim benefits can be classified as a vulnerable consumer and may not be able to access credit, or where they can access the payday lending industry, may be subject to unscrupulous lending practices and debt traps.

Further, and one would argue a rather pressing issue is that, whilst a creditworthiness assessment aims to prevent loans being taken out to pay other loans, this does quite the opposite. The government can provide a budgeting loan for the individual to pay off other loans, as it states it can be used for repayment of purchase hire loans or loans used to purchase a number of items such as furniture or household goods. One would say that surely it is not appropriate for the government to be advocating those who receive benefits to take out a loan to simply repay another. Those who are financially vulnerable due to a lack of financial education and managing finances, mentally ill or simply vulnerable due to a young age, could be granted these budgeting loans if they receive benefits, and think that it is okay for them to take out loans to repay other loans. One would argue that this is

[196] ibid

something the government needs to reconsider, offering a no interest loan to pay off an interest loan is simply not tackling the issues consumer credit raises.

The government has taken a step in the right direction with the introduction of budgeting loans, however those consumers who are subject to the protection of the responsible lending rules and can fall through the gaps in the protection they provide, are not eligible for such loans. This is a mere demonstration of the government being ignorant, more is needed to be done by the government to resolve these prominent issues. One would question why the government cannot introduce financially vulnerable criterions to incorporate the financially vulnerable into these budgeting loans. The government has already provided a structure, and whilst deciding upon criteria for those to satisfy the financially vulnerable may be rather difficult, one would say that it is far from impossible.

It is interesting to once again discuss the paternalistic element here, and how far the government should go. One would say that it is apparent that access to credit allows an individual a level of responsibility and independence, and stricter protection would lead to self-exclusion, and fewer people being able to access credit. However, if access to credit cannot be evenly balanced with consumer protection without the financially vulnerable falling through the lenient protectionist measures, a scheme should be offered with strict criteria, with the government showing a level of paternalism to ensure the financially vulnerable can access credit in a safe and affordable manner.

In a recent study, the FCA have identified that the market for alternatives to high-cost credit is failing to achieve the beneficial nature that it set out to achieve.[197] One would argue that this statement is truly correct. There are alternatives out there, however they have been

[197] Financial Conduct Authority (n 82) 15

underused, underfunded and more focus needs to be placed on these to allow the right balance between access to credit and consumer protection. However, this balance cannot be achieved through the responsible lending rules alone. If the payday loan industry wants to survive without being subjected to very strict regulations, alternative methods of credit are key to offering the financially vulnerable access to the credit that they ultimately need, without being subjected to big credit firms taking advantage of their vulnerabilities.

Government implemented schemes

Whilst it is easy to say that improving credit unions or developing budgeting loans would be a step forward in solving the issues caused by the lack of consumer protection under the responsible lending rules, it is apparent that the UK was not the only country to experience these issues. It is interesting to see how other countries have dealt with these issues and whether the methods they used to tackle such issues would be beneficial for the government in England and Wales to consider. The discrepancies highlighted with the current UK rules and regulations demonstrate that there is a need to look at new ways to provide greater access to more affordable credit, which provide safety nets for the most financially vulnerable. One way to tackle such issue would be to look at international examples of no and low interest consumer credit schemes. One suggestion is to explore how different countries tackle the same issue and determine whether a similar scheme would be advantageous to the financially vulnerable sector in the UK. Providing this sector with access to credit without exposing them to unscrupulous practices, and financial debt traps which have the potential to take over the consumers lives.[198]

[198] Laura Rodrigues, '*Payday Loans the next generation'* Step Change Debt Charity (2016) 20 >https://www.stepchange.org/Portals/0/documents/Reports/Payday-loans-next-generation.pdf < 02 August 2019

Similarly to the UK, Australia was concerned that access to short term credit lacked regulations that were strong enough to protect consumers from over indebtedness caused by such loans.[199] The ultimate issue found in Australia was that low income households were taking on a great amount of debt in order to sustain an acceptable way of life.[200] The development of uniform regulations over payday lending has developed similar trends in an array of countries, particularly similar are Australia and the UK. Many factors led to the need for very targeted new rules and regulations in Australia, however the rise of the high cost short term credit market, as well as politicians and customer advocates paying very close attention to the rest of the world, particularly the UK, highlighted this need.[201] Additional strategies were implemented alongside these reforms to reduce consumers reliance on payday loans, these strategies included the increased availability of affordable credit, as an alternative to payday loans.[202]

It is interesting to find that the Australian government supports a No Interest Loan Scheme, which provides people who receive low incomes, fair loans which are a safe and affordable alternative to payday loans.[203] Calls for regulation in Australia led to reforms which were followed by a highly charged and polarised debate, sparked by conflicting interests of consumer and welfare advocated who demanded an increased protection for consumers as well as the payday loan industry.[204] This scheme provides individuals and families on low

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[199] Gail Pearson, Richard Batten, *'Understanding Consumer Credit Law: A practical guide to the National Consumer Credit Reforms'* (CCH Australia Limited, 2010) 18
[200] Packman (n 102) 83
[201] Ibid 74
[202] Paul Ali, Cosima McRae, Ian Ramsay, *'The Politics of Payday Lending Regulation in Australia'* (Monash U L Rev, 39, 2013) 411 >https://0-heinonline-org.serlib0.essex.ac.uk/HOL/P?h=hein.journals/monash39&i=421. <accessed 13 August 2019
[203] Rebecca Wringe, *'No Interest Loan Scheme'* (NILS)' >https://goodshepherdmicrofinance.org.au/services/no-interest-loan-scheme-nils/ >accessed 02 August 2019
[204] Ali, McRae, Ramsay (n 202) 411

incomes with access, safe and affordable credit.[205] This scheme is run by community organisations in partnership with financial institutions.[206] Good Shepard Microfinance works alongside the National Australia Bank, and offers a series of credit products, specifically the No Interest Loan Scheme.[207] Loans are available to consumers for up to $1500 for essential goods such as essential household items, educational essentials and some medical services.[208] The eligibility criteria provide that to apply for a loan the individual must be on a low income of no more than $45,000 per year or a no more than a joint income of $60,000 per year[209]. Further the loans cannot be used for cash, rent arrears or debt consolidation. Once a loan is granted, repayments are set up for the individual, set at an affordable amount over twelve to eighteen months.[210]

The criteria set for these loans to be available is very interesting and one would argue a great way to allow credit for those on low incomes or financially vulnerable. When comparing this scheme to the budgeting loans offered in the UK, it is apparent that they share many similarities. Both can be used to purchase essential household items, both provide interest free loans, however the stark contrast is that to be eligible for a budgeting loan the individual must be receiving a form of benefits from the government. However, the No Interest Loan Scheme in Australia provides loans for those earning an income, allowing those on a low income, who may struggle to afford necessary items at a given time, the opportunity to access credit which is not subject to high cost and high interest. Further Australia restricts their loans to certain items and specifies that they cannot be used to

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[205] NILS, '*The No Interest Loan Schem*e' >https://nils.com.au <accessed 28 August 2019
[206] Fairweather, O'Shea, Grantham (n 25) 120
[207] Buckland (n 98) 162
[208] NILS (n 205)
[209] ibid
[210] ibid

repay other loans. This is a much better improvement than that provided by budgeting loans. It allows finance to individuals for items that are essential at a particular point in time, it does not push forward a culture of taking out loans to repay other loans. By limiting what the loans can be used for allows consumers to take out loans for essential items, as opposed to luxury items they want, rather than the items they ultimately need. Further, unlike budgeting loans this level of paternalism is needed, instead of promoting interest free loans with the allowance for them to be used to repay existing loans, an interesting point that one suggests the government in the UK should take into consideration.

An evaluation of the no interest loan scheme demonstrated that they have been successful in diverting consumers from fringe credit, with forty-two percent of no interest loan recipients ceasing to borrow from such lenders.[211] Further, and more recently, the headlines have featured Australia's plans to pour sixty-million pounds into the no interest loan scheme to divert vulnerable borrowers from high interest payday lenders.[212] It is believed that the policy is a modest and sensible investment in helping people get loans to help them make ends meet when they need it, without having to turn to payday lenders.[213] Evidence suggest this scheme has been successful and one would argue that it is a good way to allow loans to the financially vulnerable, with a level of paternalism, that prevents them from financial exclusion and the harm that can be associated with payday lending.

Although alternative affordable credit is favoured, it must be noted that one type of affordable credit is unlikely to be enough for everyone. There is a need for an expansive

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[211] Fairweather, O'Shea, Grantham (n 25) 120

[212] Paul Karp, '*Labour pledges $60m to divert vulnerable borrowers from payday lenders'* (The Guardian, 2019) > https://www.theguardian.com/australia-news/2019/mar/22/labor-pledges-60m-to-divert-vulnerable-borrowers-from-payday-lenders <accessed 19 August 2019

[213] ibid

provision which allows affordable credit alternatives and emergency support for people who need access to credit immediately.[214] Debt charity StepChange recommended that a sustained and long-term programme is necessary to expand community lending, further they have identified that the UK lead the development of a no interest loan provision as an alternative to payday lending, for the financially vulnerable.[215]

<u>Conclusion</u>

From this research, it is practicable to conclude that whilst the introduction of the responsible lending rules has been a step forward in ensuring consumers are protected when considering a payday loan, financially vulnerable consumers are falling through the safety net they provide. A big issue is the FCA's attempt to balance consumer protection with access to credit. The current regulations in place delve away from consumer protection to allow for individuals to be able to access credit, and whilst the FCA has emphasised its flexible approach to the regulations and the guidance it provides, it is rather abstract to ensure credit lenders adopt their own assessments tailored to their products and services. However, the problem with allowing this level of flexibility subsequently subjects the financially vulnerable sector of society to loopholes and gaps in the legislation where harm is likely to be caused to them. Strictly keeping many elements as guidance and not enforcing this guidance as regulation, provides scope for firms to disregard the consumer protectionist elements, and further makes the regulations difficult to enforce.

However, if these rules were more prescriptive and enforced in a more strict manner, consumer protection would override access to credit and take away the benefits that it

[214] StepChange (n 178)
[215] ibid

provides, such as financial inclusion, the ease of accessing credit and the level of dignity and independence the provision purports. Balancing access to credit and consumer protection for the financially vulnerable is seemingly impossible, as increasing one jeopardises the effectiveness of the other.

An analysis of the responsible lending rules demonstrates that there are problems with them from a consumer protection perspective. The FCA's use of terminology takes a very relaxed approach and again provides scope for credit lenders to abuse their power and grant loans to consumers even where the creditworthiness assessment is not fully fulfilled. Again, similar issues arise with regard to the affordability assessment. The lack of restrictive measures provides a level of scope to credit lenders to abuse their powers and take advantage of consumers vulnerabilities. This is clearly demonstrated through firms claiming to be unsure on how to interpret some of the terminology used by the FCA, and the FCA's refusal to be more prescriptive simply results in lenders being confused and unsure, a position one would argue that a firm should not be in when deciding whether or not to grant a loan. Further issues are raised by CRA's. Their lack of real time data sharing poses a problem for firms, as it leaves them with out of date information, potentially attributing to unaffordable debt and having quite the opposite effect to protecting consumers.

The FCA provides a good consumer protectionist regulation with its affordability assessment, however, again provides scope for lenders to easily abuse such regulation. Further, the use of abstract terms is very confusing. The interpretation of terms and phrases are likely to differ from firm to firm, again providing that leeway and scope for credit lenders to abuse the consumer protection regulations. The case study of Wonga is the perfect example of a credit lender wo abused the level and scope provided by the FCA and failed to carry out adequate affordability assessments.

It is clear to see that providing alternatives to payday lending would avoid the difficulty of balancing access to credit with consumer protection and allow the financially vulnerable a better way of getting the credit they need, without being subjected to financial exclusion. Credit unions provide a good start as an alternative, advertising and emphasising their use would be a step forward in making people aware of the alternatives that are available. Further, they provide a good structure for the government to introduce something similar, specifically focussing on the financially vulnerable. Budgeting loans again are a good alternative for the people who meet its criteria, however one would recommend that the government revise the use of these loans and ensure better effectiveness of their use, for example not being used to repay loans taken out for luxurious items. They provide a good starting point once again, they offer a set-criteria, no interest and emphasise that the government has acknowledged the issue of people on low incomes being able to access affordable credit. However, the government needs to further acknowledge that low income is not the only source of financial vulnerability, and incorporating elements such as mental health, age and employment issues into such a scheme is likely to be a great way of offering alternatives to high-cost credit.

It is interesting to see how the Australian government dealt with a similar pressing issue. Their no interest loan scheme has focussed on key issues and set a practical list of criteria for people who genuinely need these loans, to be able to access them. The scheme has been proven to be a successful alternative for Australia, and whilst one would say what works for one country may not work for another, it is worth the government in England and Wales analysing this government supported scheme and develop ideas to tackle the issues that still remain in the UK today.

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