EXPLANATORY MEMORANDUM TO

THE FINANCIAL SERVICES AND MARKETS ACT 2000 (OMBUDSMAN SCHEME) (CONSUMER CREDIT JURISDICTION) ORDER 2007

2007 No. 383

1. This explanatory memorandum has been prepared by the Department of Trade and Industry and is laid before Parliament by Command of Her Majesty.

2. Description

2.1. The Financial Services and Markets Act 2000 (Ombudsman Scheme) (Consumer Credit Jurisdiction) Order 2007 ("the Order") specifies the types of business for the purposes of section 226A(2)(e) of the Financial Services and Markets Act 2000. Complaints satisfying certain conditions may be made to the Financial Ombudsman Service about acts or omissions that have occurred in the course of a business of a type so specified.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1. None

4. Legislative Background

4.1. Section 226A of the Financial Services and Markets Act 2000, as inserted by the section 59 of the Consumer Credit Act 2006, provides for the consumer credit dispute resolution scheme of the Financial Ombudsman. The Order specifies certain types of business, which are brought within the jurisdiction of the scheme.

5. Territorial Extent and Application

5.1. This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

6.1. As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

7.1. The Consumer Credit White Paper of 2003 set out the Government Agenda for change in the consumer credit market. The Consumer Credit Act 2006 continued the aim of enhancing consumer redress, improving the regulation of consumer credit businesses and ensuring that regulation is appropriate. The impact of this Order was considered as part of the Regulatory Impact Assessment (RIA) that was conducted for the Consumer Credit Bill published in November 2004.

7.2. The new section 226A of the Financial Services and Markets Act 2000 provides for the consumer credit jurisdiction of the Financial Ombudsman scheme. The Order specifies the types of business for the purposes of this section and brings them within the jurisdiction of the scheme. Complaints may only be made to the Ombudsman about acts or omissions that have occurred in the course of businesses of these types.
The list of types of businesses includes two new licensable activities, credit information services and credit reference agencies.

7.3. If they have a complaint about one of the types of business coming under the jurisdiction of the Financial Ombudsman scheme, consumers will be able to complain directly and at no cost to an independent adjudicator.

8. Impact

8.1. The Office of Fair Trading estimated that in 2000 the consumer detriment to consumers in all consumer transactions was about £8.3 billion per annum, a significant element of which is likely to be in the consumer credit market. The Consumer Credit Act 2006 is bringing in a raft of measures, which will bring direct or indirect benefit to consumers, and help address consumer detriment.

8.2. Two of these measures are the Office of Fair Trading's new consumer credit licensing regime, and the introduction of the consumer credit alternative dispute resolution scheme of the Financial Ombudsman Service. The associated costs of these measures have been considered as part of the Regulatory Impact Assessment conducted for the Consumer Credit Bill, the relevant sections of which are attached as an annex to this Explanatory Memorandum.

8.3. The additional direct licensing costs arising from the Consumer Credit Act 2006 for all consumer credit businesses are estimated to be £18 - £26 per licensee for sole traders (40% of licensees), and £44 - £66 per licensee for other businesses. Consumer credit licences will be required for two new types of business that were not previously required to hold them; credit information service businesses and credit reference businesses.

8.4. All consumer credit businesses will need to devote resources to having processes in place to comply with the consumer credit customer redress scheme operated by the Financial Ombudsman Service. There will be a cost to consumer credit businesses for the Financial Ombudsman Service levy, costs involved with complying with the processes laid out by the Financial Ombudsman Service, and a fee for any cases brought against them. The estimated total additional cost to consumer credit businesses of compliance with the Financial Ombudsman's scheme is estimated at £3.6 - £5.3 million per year. (RIA s.13.8, s.36, s.43.5, s.44.2, s.45.3)

8.5. Bringing consumer credit businesses under the consumer credit jurisdiction of the Financial Ombudsman scheme means consumers will have an improved ability to seek and obtain redress. (RIA s.31.5, s.21, s.40.3)

9. Contact

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Annex to Explanatory Memorandum

Consumer Credit Bill

Full Regulatory Impact Assessment - extracts relevant to Financial services and Markets Act 2000(Ombudsman Scheme) (Consumer Credit Jurisdiction) Order 2007

The cost of alleged non-compliance:

13.8 If a consumer credit business is the subject of:

(a) OFT action in relation to licensing issues; or

(b) a complaint that leads to redress action by a consumer,

then the business may incur one or more of the following costs: (i) the cost of dealing with OFT requests for additional information; (ii) legal fees and other associated costs in respect of OFT licensing proceedings; (iii) a financial penalty, if the business breaches a licence requirement; (iv) an ADR case fee, if the consumer redress action is dealt with by ADR[34]; (v) court costs, legal fees and other associated costs, if the consumer redress action is dealt with by a court; (vi) compensation payments, if a consumer claim is upheld against the business by either the ADR adjudicator or the court[35].

Summary and Recommendations

21. Improving consumer rights and redress: Option, Cost, Benefit

21.1: Do nothing

Cost: No additional costs

Benefit: No additional benefits

21.2: Reform extortionate credit test and introduce a compulsory ADR

Cost:

Total cost of the ADR levy – c.£1-2 million. Costs for business in complying with complaints handling standards, dealing with additional complaints and the ADR process. Lenders will face the cost of transferring to consumers the money they had gained as a consequence of unfairness. A larger number of consumers will incur costs in pursuing complaints. Advice

[34] Following consultation with the industry group on credit repair, we estimate that there are up to 100 such businesses who will need a licence, of which some may already have a licence, if they also undertake other licensable activities, such as debt-councelling.

[35] The first two complaints to FOS will be free to the consumer credit business.

providers may face costs in bringing more complaints to ADR and the courts, in training staff and educating consumers.

Benefit:

New test of unfairness and the opportunity for consumers to go to ADR will improve conduct of lenders in the market, thereby reducing consumer detriment in the market that currently amounts to hundreds of millions of pounds. Reduction in costs to each individual consumer of making complaints. Consumers will benefit from a transfer from lenders of the money paid to lenders as a consequence of unfairness. Effective competition in the market will be improved. Reduce costs to business of dealing with complaints by enabling them to be dealt with by non-legal means.

22. Improving regulation of the consumer credit business

22.3: Voluntary code

Cost:

The costs for businesses would be about half of those for option 2. Consumer detriment would also be higher than under option 2, and reduced only slightly from the current situation.

Benefit:

Benefits would be similar to those derived under option 2, but of a smaller magnitude since they would only be felt by clients of those businesses who had signed up to the code. We estimate that the benefits would be around half of those under option 2.

Option 3: Introduce voluntary codes of practice with new standards of conduct and dispute resolution procedures

31. Costs

Option 1: Do nothing.

31.1 Option 1 would not impose any additional costs on business. Consumer detriment resulting from the current situation would continue.

Option 2: Reform the extortionate credit test and introduce a compulsory ADR system.

31.2 Replacing the 'extortionate' credit test and introducing a compulsory ADR system would mean that all consumer credit businesses would be required to pay for the scheme, through a levy. This levy would be modest and would cover the basic administration costs of the scheme. It is estimated to cost between £10-£20 per licence.

31.3 Consumer credit businesses could also incur some indirect costs in terms of modifying or improving existing compliance and complaint handling systems. For many consumer credit businesses these costs will represent an incremental increase,
although some will incur additional costs in developing these systems.

31.4 Option 2 would also mean that consumer credit businesses could incur indirect costs, arising out of alleged non-compliance with the reformed Act. Not all businesses would incur such costs, as the vast majority is compliant. These indirect costs could include:
(a) a system which facilitates consumer enquiries and complaints will mean that consumer credit businesses: (i) could be required to dedicate additional resources to
complaint handling; and (ii) would be required to meet specific complaints handling standards, which is a consequence of the requirement for consumer credit businesses to submit to ADR[50];
(b) in cases that are determined by ADR, those consumer credit businesses which are found to have acted in a manner which are found to have acted in a manner which is not 'fair and reasonable' could face the possibility of compensating consumers, e.g. changes to terms of the agreement or repayment schedules, an apology, additional services or financial compensation (this will represent a direct transfer from business to consumers).

31.5 Replacing the 'extortionate' credit test and introducing a compulsory ADR system would result in the following costs to consumers:

[50] We propose that submitting to ADR will be a mandatory condition of fitness to hold a consumer credit licence, and that FOS will require standards similar to those required by FSA - in respect of complaint handling systems.
(c) in cases determined by courts under the unfair credit test, consumer credit businesses who are found to have behaved 'unfairly' could face the possibility of compensating consumers, e.g. changes to terms of the agreement or repayment schedules, financial compensation and the payment of legal costs (this will represent a direct transfer from business to consumers); and
(d) as a consequence of a regime that encourages a general standard of conduct, consumer credit businesses will incur costs in ensuring internal compliance with the Act, in terms of training staff and auditing systems.
(a) an improved ability to seek and obtain redress may encourage more consumers to do so. This will mean that more consumers will incur costs in making those enquiries
both to consumer credit businesses and to the ADR provider (although those who are successful may receive compensation and offset these costs);
(b) advice providers could also incur additional costs in: (i) bringing a higher number of more effective complaints to ADR and to courts; (ii) training staff and educating consumers about the new options open to consumers.

(a) an improved ability to seek and obtain redress may encourage more consumers to do so. This will mean that more consumers will incur costs in making those enquiries both to consumer credit businesses and to the ADR provider (although those who are successful may receive compensation and offset these costs);
(b) advice providers could also incur additional costs in:
(i) bringing a higher number of more effective complaints to ADR and to courts;
(ii) training staff and educating consumers about the new options open to consumers.

31.6 There is also a possibility that in some sectors of the market the changes will mean that the cost of borrowing may increase slightly, to reflect the initial increase in the risk to consumer credit businesses of challenges. This could result in some costs being passed on to consumers. However, we anticipate that these costs will be negligible when considered over the whole consumer credit market, because business will also have significant incentives to comply with the reformed Act and thus reduce this risk[51].

Option 3: Introduce voluntary codes of practice with new standards of conduct and dispute resolution procedures.

31.7 We estimate that this option would result in business incurring about half of the costs of Option 2, for the reasons set out in paragraphs 30.4-30.6 above.

31.8 It would also mean that consumers would continue to suffer a higher degree of detriment than they would under Option 2, because the level of consumer protection and rights of redress would be lower.

32. Our preferred option
32.1 On the basis of the benefit and cost analysis set out above and our consultations with stakeholders, our preferred option is Option 2: reform the extortionate credit test and introduce an ADR system.

[51] These costs should also be balanced against the increased certainty that lenders will enjoy as a consequence of the amendments to subs.127(3)& (4) Act; see para.53.4 below.
Option 3: Introduce voluntary codes of practice with new standards of conduct and dispute resolution procedures.

33. Costs for a typical business

33.1 The cost of compliance – A typical consumer credit business would incur direct costs in relation to the payment of a levy to fund the ADR scheme50 and may incur indirect costs in relation to training staff and maintaining and auditing compliance with the reformed Act. Direct costs would represent an incremental cost to business.
Indirect costs could represent an incremental cost to businesses where they already have complaints handling and compliance systems in place, and an additional cost for those that do not.

33.2 We estimate that all consumer credit licensees will incur additional direct compliance costs of between £10 and £20 per year for the ADR levy.

33.3 The cost of alleged non-compliance – If a consumer credit business is the subject of a complaint that leads to redress action by a consumer, then the business may incur one or more of the following costs:
(a) an ADR case fee, if the consumer redress action is dealt with by ADR;
(b) court costs, legal fees and other associated management costs, if the consumer redress action is dealt with by a court; and
(c) compensation payments, if a consumer claim is upheld against the business by either the ADR adjudicator or the court.

These are the costs of alleged or actual non-compliance with the reformed Act. The vast majority of businesses are compliant and will remain so, and will not have to incur these costs. The scale of 50 FOS has estimated that the levy will be about £10-£20 per annum per business.

34. Business sectors affected

34.1 The effect of the cost of compliance – All consumer credit businesses would incur the direct costs of the new ADR scheme, which we estimate will cost c.£1-2 million per year[53]. Those that do not now have any compliance and complaints handling systems or a sufficient system in place may incur an increase in indirect costs resulting from the changes. The costs

[53] Based on 106,000 active consumer credit licensees paying between £10 and £20 each.

of compliance will fall more heavily on those businesses with undeveloped or non-existent compliance and complaints handling systems.

34.2 The effect of the cost of alleged non-compliance – As we have said above, the vast majority of businesses are compliant and will incur no costs associated with non-compliance. However, some business sectors may be more exposed to costs of alleged non-compliance than others. The potential for redress action will largely be confined to lenders and finance brokers, as non-compliance by these businesses is the most likely source of significant harm to consumers in respect of credit. Furthermore,
the potential for redress action may increase where consumers are more vulnerable to unfairness or exploitation in a particular sector.

36. Consultation with small business: the Small Firms Impact Test 36.1 The consumer credit industry involves many small firms: 40% of all licensees are sole traders, and 55% of all licensees employ less than 10 people[24]. We have consulted, and continue to work with trade associations representing small firms and their members (see 20.2 Public Consultation above). We aim to avoid undue burdens on small business, and balance the costs of the reforms with the benefits of consumer protection. 36.2 Small firms have expressed some concern over the costs of compliance with the reformed Act. They have also expressed concern that they will face high costs in relation to ADR, if there is a large number of cases brought by consumers. This risk will be mitigated by FOS's proposal to waive the case fee for the first two cases brought against a firm per year: small firms are unlikely to face many more than two cases, so they will not incur substantial costs[55].

36.3 If a business is the subject of a lot of cases in proportion to the level of its consumer credit activity then this could suggest non-compliance with the Act, and also leave it open to licensing action. The ADR mechanism will filter complaints carefully before taking them on as cases, to ensure that they are not frivolous or
vexatious. Consumer credit businesses will also be assisted by OFT guidance on licensing and enforcement.

[54] Source: MORI research on consumer credit licensees
[55] Source: Mori research on consumer credit licensees: 93% of licensees receive two or fewer complaints.

Licensing

40.2 We have set out in Part 1 above an indication of the scale of consumer detriment that results from the behaviour of consumer credit businesses. OFT, in enforcing the Act, is constrained in its ability under the licensing regime to address in a proportionate way trading practices giving rise to consumer detriment (i.e. behaviour which might not be sufficiently poor to mean that a business may be unfit to hold a licence). If allowed to persist, this could lead to consumers losing trust and confidence in the market and potentially damage the businesses of reputable traders.

40.3 We have identified the following weaknesses in the Act's licensing regime:

(a) the current test of fitness is limited in that it is essentially backward looking, requiring OFT to give particular weight to past conduct, rather than looking forward and considering the competence of the business to provide credit and credit services. Since past behaviour is not always the best indicator of future behaviour, this may allow potentially unfit traders to enter the market;

(b) it does not allow OFT to take a risk-based approach (including a "light touch" approach for low-risk businesses) and apply a more stringent approach where there are risks to consumers;

(c) the sanctions available to OFT where the fitness of the applicant or consumer credit business is in doubt are not always adequate. At present, OFT may only refuse an application for a licence, grant a licence on different terms or revoke, vary or suspend a licence. For example, a consumer credit business may cause consumer detriment due to the activities of a small part of its business, but remain fit to hold a licence when the business is considered as a whole.

43. Costs

Option 1: Do nothing.

43.1 Option 1 would result in no additional costs.

Option 2: Deregulation.

43.2 The costs of running the regime for OFT, and the costs of complying with it for business would be lower than for the other options. However, the costs for consumers would be higher than under any other option because the absence of regulation would increase scope for unscrupulous operators. Reputable consumer credit businesses would also face the cost of lower consumer confidence in the market.

43.3 In particular:

(a) the current level of consumer protection would decline because any person could enter the consumer credit market without scrutiny. Regulation would be purely reactive, as problems would have to be manifest before any action could be taken. Thus, those who handle consumers' money, tie consumers into serious commitments (including loans secured on their homes), and collect debts would be free to operate without checks until the problems they cause came to light;

(b) without the confidence that OFT has screened consumer credit businesses, consumers may incur additional costs in determining their fitness. The loss of consumer protection in this area, whilst other reforms to the Act to improve protection are underway, could confuse consumers, and undermine the effectiveness of the other reforms;

(c) consumers would be much more likely to suffer detriment resulting from agreements provided by unfit consumer credit businesses. They would have to pursue redress using the ADR system or the courts.68 If there were no licensing regime to exclude unfit consumer credit businesses, the number of complaints might increase by 10-25%[71];

(d) the retention of the licensing system also allows lenders to have some confidence in the fitness of those other consumer credit businesses, such as brokers and debt collectors, with whom they deal. Abolishing the licensing system would increase the burden on business to ensure that other consumer credit businesses with whom they deal were reputable because they would lack an objective record of licensed businesses and it would take considerably more time to determine another business's bona fides;

(e) without a licensing system, the ADR would have no list of consumer credit businesses on which they could raise a levy and would therefore increase the case fee to cover its costs, imposing additional costs on business[72]. Administration of

[71] This gives a total of between c.11,300 and c.12,900 cases per year. Assuming each case costs £550, this means an additional cost of c.£0.6 million to c£1.4 million per year

[72] The case fee would rise to approximately £550 (the cost per case to FOS).

the ADR might also be more difficult, because it could not rely on the list of consumer credit businesses, but rather would have to be made a compulsory mechanism for consumer credit cases;
(f) fit consumer credit businesses would suffer from the loss of consumer confidence in the market and businesses would face increased uncertainty about what was required of them; and
(g) OFT would also lose information it holds currently about traders, which can help in targeting guidance.

Option 3: Proportionate Regulation.

43.4 The costs to OFT and for business in complying with this regime are higher than for the other options. However, Option 3 provides the greatest reduction in consumer detriment.

43.5 The costs of the reformed licensing regime would be:
(a) increased licence fees for business. With c.106,000 active consumer credit licensees[73], the change in the cost of the licensing regime will translate into a modest sum for most businesses, which we estimate at £18-26 for a sole trader and £44-66 for any other business[74];
(b) possible higher costs of information provision to OFT under the strengthened licensing regime, where the risk assessment or concerns over competence mean that more information is needed to establish fitness[75];
(c) the cost of compliance is not expected to rise for fit businesses, which currently comply with existing guidelines[76]. OFT's guidance on the new fitness test, will explain the requirements, and how the standard of fitness will be assessed. This guidance will be consulted upon and will be available in good time before the reforms come into force, to give business time to prepare;
(d) costs for previously unlicensed businesses providing credit information services and debt administration businesses in becoming licensed (licence fee and costs of compliance); and

[73] MORI estimates there are 105,932 consumer credit businesses, based on 125,000 licences in use and an average of 1.18 licences per business.
[74] We estimate that the additional direct licensing costs for typical businesses will be as follows: for a typical sole trader, which represent 40% of consumer credit licensees, an increase to the current 5-yearly licence fee of c.£110 of 80-120%, giving a yearly increase of c.£18-26 per licensee; and for any other business, an increase to the current 5-yearly licence fee of c.£275 of 80-120%, giving a yearly increase of c.£44-66 per licensee.
[75] The information requested will be of the sort that is readily available to businesses, so no collection costs will be imposed on business. Formal powers of investigation will be exercisable only subject to tests detailed on the face of the Act, and OFT and FSA will share information.
[76] It is estimated that around 1-2% of the licensing population will be subject to further investigation, and will therefore incur the additional costs (e.g. costs of providing further information) related to this.

(e) costs for OFT (and Trading Standards Departments) in running the new licensing regime. It is proposed that over a five-year transitional period, new indefinite licences will be issued, as each licence comes up for renewal. The costs to OFT of running the new licensing regime are therefore expected approximately to double to a peak of around £12m per year in the fifth year of operating the new regime, and thereafter to fall[77]. There will also be some implementation costs for OFT in designing the new licensing structure, preparing and publishing guidance and staff training. These are estimated to be around £500,000.

44. Costs for a typical business:

44.1 The cost of compliance - The proposed reforms mean that a typical consumer credit business will incur direct costs in respect of compliance with the requirements of licensing system and the provision of required post-contractual information (such as annual statements and arrears notices).

44.2 Licensing costs: We estimate that the additional direct licensing costs for typical businesses will be as follows:
(a) for a typical sole trader, which represent 40% of consumer credit licensees, an increase to the current 5-yearly licence fee of c.£110 of 80-120%,86 giving a yearly increase of c.£18-26 per licensee.
(b) for any other business, an increase to the current 5-yearly
licence fee of c.£275 of 80-120%,87 giving a yearly increase of c.£44-66 per licensee.

45. Business sectors affected:

45.1 The effect on business of the cost of compliance - All business sectors in the consumer credit market will incur the costs of complying with the Act. These costs have been identified above. The direct costs of compliance with the licensing regime apply to all consumer credit businesses (albeit at varying levels) and in most cases will represent an incremental increase to current costs of compliance (although credit information service providers and debt administrators, who do not currently require a licence, will face this new cost)[91]. Costs in relation to post-contractual disclosure will be incurred by lenders and not by intermediaries.

[77] These costs (funded by the licence fees) will rise incrementally from the current £6m cost over the five years in which existing licences will be renewed according to the new test, and then will fall
[91] Following consultation with the industry working group on credit repair, we estimate that there are up to 100 such businesses who will need a licence, of which some may already have a licence, if they also undertake other

45.2 In terms of OFT's oversight of licensing, there are sectors that may, because of a potential for increased consumer detriment in those sectors, be the subject of additional OFT scrutiny in relation to fitness to hold a licence and also may be required to operate subject to certain conditions which may result in increased costs.

45.3 Based on the current number of active consumer credit licences, we estimate that the total additional cost of direct of compliance to consumer credit businesses will be:
(a) c.£0.8 –1.1 million per year for all sole traders[92]; and
(b) c.£2.8 – 4.2 million per year for other businesses[93].

giving a total additional cost of direct compliance with the new licensing regime to business of c.£3.6 – £5.3 million per year. This amount will be in addition to the c.£6 million currently paid annually for consumer credit licences.

45.4 We estimate that the cost to small business of introducing the new post-contract information requirements would be a one-off cost to all small businesses c.£1.1 million.

ANNEX

Consumer Credit: Indicating the scale of consumer detriment in the United Kingdom

1. The basis of this analysis:

1.1 OFT estimated that in 2000 the consumer detriment to all consumers in all consumer transactions was about £8.3 billion per year[104]. Consumer detriment in the consumer credit market is likely to be considerable, given the problems that many consumers face in terms of poor transparency and unfair practices by a small, but significant,
proportion of consumer credit businesses.

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licensable business, such as debt-counselling. We also expect that many debt administrators will already have a debt collection licence or consumer credit business licence.
[92] Based on 40% of 106,000 active consumer credit licenses (c.42,000) multiplied by £18-26
[93] Based on 60% of 106,000 active consumer credit licenses (c.64,000) multiplied by £44-66. This is based on the current incorporated body licence fee of £275. Under the reforms, OFT will have the power to vary licence fees according to the size of the applicant or licensees business or the nature of that business.
[104] OFT Consumer Detriment April 2000. OFT imposed significant qualifications on this figure.

1.2 This analysis does not seek to quantify consumer detriment in the consumer credit market. Any accurate assessment of this would be extremely difficult to calculate, even on the best information available.
Rather, it seeks to indicate the scale of total consumer detriment in relation to those consumers who make enquiries to free advice providers and government bodies such as OFT and, where relevant, FOS and FSA.

1.3 This analysis does not factor in the consumer detriment for those:
(a) who cannot or do not make an enquiry;
(b) who pay excessive credit costs because they can afford to and who choose either not to make an enquiry or do not know that that can do something about the problem; and
(c) who obtain paid debt advice from a solicitor, accountant or debt management company.

2. The nature of consumer credit problems

2.1 We estimate that c.80% of consumers who bring enquiries to free advice providers have a general enquiry or are seeking advice on how to deal with problems arising from multiple borrowing, and do not dispute their liability for the debts they have[105]. Therefore, we estimate that c.20% of consumers are enquiring about a potential issue of unfairness or exploitation (which could relate to either general or specific issues concerning the consumer credit business's conduct in selling, making or administering the credit agreement). However, within the c.80% who do not dispute liability, we estimate that a further c.10-15% of consumers could have an substantive issue relating to irresponsible lending that has led to the situation escalating to the point of crisis[106]. This means that c.35% of the 600,000 consumers who make an enquiry to a free advice provider, or c.210,000, could be affected by potentially unfair conduct. This percentage should not be applied to all consumers who obtain consumer credit.

3. The cost of dealing with enquiries

[105] This figure is an estimate based on our review of consumer enquiries to free advice providers (see footnote 11 above). The proportion of issues that related to general debt advice and managing multiple debt was uniformly high for all free advice providers that we visited.
[106] Again, this figure is an estimate based on our review of consumer enquiries to free advice providers (see footnote 11 above). The proportion of issues that related to general debt advice and managing multiple debt and which involved an issue of potential irresponsible lending was, small but significant in all sets of files we examined.

3.1 In the White Paper we estimated that the cost to all consumers of simply making enquiries is c.£40 million a year[107]. On the basis that c.35% of people who make enquiries have a substantive issue to be dealt with, the cost to consumers of making enquiries would be c.£14 million a year[108]. Additionally, we estimate that the cost to free advice providers of dealing with these enquiries was well in excess of c.£60 million in 2003-2004[109]. We do not think that this figure will change in the short term, and we note that the demand for money advice currently outstrips supply.

4. Indicating the extent of consumer detriment.

4.1 The direct detriment to consumers from unfair lending practices is made up of such things as:

(a) the cost of purchasing products that are not necessary or suitable for the consumer, but purchased because of misleading or high-pressure sales tactics;

(b) excessively high interest payments; excessively high fees and charges payable on default and default interest;

(c) costs associated with the provision of inappropriate ancillary products[110];

(d) costs incurred by lenders in relation to recovery (i.e. debt collection and legal costs) and interest applied to those costs;

(f) costs to the consumer associated with resolving issues and remedying the situation, including advice and legal costs; and

(g) costs flowing from the time and stress that the dispute causes.

4.2 In some cases these costs may result from specific unfair conduct by a consumer credit business. In other cases, the weaknesses of the existing law may have encouraged unfair lending practices by a lender or a number of lenders to be regarded as acceptable, and mean that a potentially large number of consumers pay more than they would otherwise. The fact

[107] See para.1.39 of "Fair, Clear and Competitive – The Consumer Credit Market in the 21st Century" White Paper (2003). This is based on the methodology used by OFT in its paper entitled Consumer Detriment (2000). The detriment figure is based on the number of complaints received regarding credit agreements and includes all the potential costs incurred by the consumer in complaining. These include legal and advice costs, telephone and stationery costs, the use of personal time and lost earnings etc. See table 6.5 of OFT paper for a fuller exposition of the costs included.

[108] However, we estimate that the actual cost of making such substantive enquiries would be much higher, reflecting the additional effort and expense to the consumer of pursuing a substantive complaint.

[109] This is composed of c.£970,000 for Citizens Advice Scotland, c.£18 million for Citizens Advice (England & Wales), c.£38 million for advice providers covered by Advice UK. The bodies concerned have provided these estimates. This does not include the cost to OFT of dealing with consumer enquiries and complaints. This information is based on data provided by the relevant bodies. The bulk of funding for these bodies comes from grants from local authorities, the Legal Services Commission and various charities and charitable trusts.

that consumers have been reluctant to challenge agreements in the courts, and currently have very few other means of effectively doing so, has served to exacerbate consumer detriment.

4.3 To quantify this consumer detriment is extremely difficult, but we can say that with the increasing volume of consumer enquiries about consumer credit problems and the increasing size of the total amount of outstanding loans, it is considerable. Having said that, we can indicate the scale of consumer detriment based on a relatively modest average level of individual detriment to those consumers who make an enquiry to a free advice provider.

4.4 This indication does not factor in the consumer detriment for those:
(a) who cannot or do not make an enquiry;
(b) who pay excessive credit costs because they can afford to and who choose either not to make an enquiry or do not know that that can do something about the problem; and
(c) who obtain paid debt advice from a solicitor, accountant or debt management company.

4.5 Assuming that:
(a) in 2003 the average level of outstanding consumer credit debt per household was £6,464[111];
(b) that at least 210,000 consumers raise a potential issue of unfairness or exploitation with free advice providers[112];
(c) and the detriment to an individual consumer is only 20% of the value of the amount of average outstanding debt, or c.£1,300, then the consumer detriment to consumers who make enquiries to free advice providers would be between c.£250-300 million a year.

4.6 This amount may not seem large in the context of the total amount lent to consumers, but the scale of individual consumer detriment can often be devastating in the context of the personal circumstances of those who have serious limitations on their finances and on their ability to manage them.

[110] n.b. ancillary insurance products has been regulated by FSA since 31 October 2004.
[111] Average debt of consumers, 2003 data from FSA. See also DTI/DWP June 2004, Tackling Over-indebtedness- Action Plan 2004, p.13.
[112] See paragraph 4.1 above.