

Regulator Assessment: Qualifying Regulatory Provisions

Title of proposal: Consumer credit – amendments to guarantor lending

Rules

Lead regulator: FCA

Date of assessment: July 2016

Commencement date: November 2017

Origin: Domestic

Does this include implementation of a Cutting Red Tape review? No

Which areas of the UK will be affected? Whole of UK

Brief outline of proposed new or amended regulatory activity

FCA Policy Statement 15/23 sets out new rules on guarantor loans. A guarantor loan is where the borrower provides security in the form of a guarantor. The guarantor undertakes to make payments under the credit agreement if the borrower does not pay, and may also indemnify the lender. The amended rules only apply to individual guarantors and borrowers (i.e. not firms).

The policy amends the Consumer Credit sourcebook (CONC) rules on guarantor lending. The amendments can be grouped under four headings:

1. Affordability assessments

- CONC 5.2.5R – to require the firm to assess the potential for the guarantor’s commitments in relation to the credit agreement to adversely affect the guarantor’s financial situation.
- CONC 6.2.1AR – to require the firm to make a similar assessment before any significant increase in the amount of credit under the credit agreement.

2. Explanations

- CONC 4.2.22R – to require the firm to provide an adequate written or oral precontractual explanation to the guarantor, covering the circumstances in which the guarantee or indemnity may be called on and the implications for the guarantor if it is. However, an independent third party (e.g. lawyer or credit broker) can also provide these explanations.
- CONC 4.6.5R – to require the firm to provide an adequate pre-contractual explanation in plain and intelligible language to the guarantor before a continuous payment authority (CPA) is granted.

3. Financial difficulty

- CONC 7.1.4R – to provide that a guarantor is to be treated as a customer for the purposes of CONC 7.3.4R (treating customers in default or arrears difficulties with forbearance and due consideration), and other CONC 7 rules on arrears, default and recovery, with the exception of provisions solely applicable to a borrower.
CONC 6.7.25AR – to extend to guarantors the requirements relating to amendments to the terms of the CPA.
- CONC 7.6.15AG – to clarify that, where a guarantor has given a CPA in relation to a high-cost, short-term credit agreement, the limit of two unsuccessful attempts on use of the CPA applies separately to the borrower and the guarantor.

4. Consumer Credit Principles

- PRIN – to clarify that a guarantor is to be treated as a customer for the purposes of Principle 6 (treating customers fairly) and Principle 7 (communications).

Which type of business will be affected? How many are estimated to be affected?

Guarantor loan providers offer loans to typically sub-prime or near-prime customers that are guaranteed by a second person, usually a family member or friend. Guarantor loans are often between £1,000 and £5,000 for a period of between one to four years (although this varies across the market). If a borrower misses a repayment, the guarantor will be called upon to make the payment. Many firms will only accept a person as guarantor if they are a property owner. The market consists of around 20 firms, one of which accounts for the majority of the market – but there has been some significant growth in market share for a number of new entrants in recent years.

Price base year	Implementation date	Duration of policy (years)	Business Net Present Value	Net cost to business (EANDCB)	BIT score
2015	2 November 2016	10	0	0	0

Please set out the impact to business clearly with a breakdown of costs and benefits

1. Affordability assessments. All the firms who responded to a survey conducted during the consultation (see additional information) indicated that they were already carrying out affordability assessments of all guarantors. While five out of nine firms responded there had been a change “in the standard/ rigour of the affordability assessments [they] carry out for borrowers since FCA regulation or otherwise”, this question does not refer to the changes being consulted on in Consultation Paper 15/6 or Policy Statement 15/23. Therefore, on the basis of the survey evidence, we assume that guarantor loan providers already carry out affordability assessments and there are negligible additional compliance costs or impacts on lending volumes.

2. Explanations. All firms that responded to the consultation survey stated that they already provide adequate explanations to guarantors and that our proposals in this area would have no impact. On that basis, we consider that the proposal is unlikely to result in costs of more than minimal significance. While there may be some bias in responses, and we cannot be certain that the level of explanation meets that which would be required by the proposed rule, we cannot quantify potential compliance or other impacts given the views expressed.

3. Financial difficulty. All but one respondent reported that they already treat guarantors as if CONC 7 rules apply. For example, all responding firms reported that they alert the guarantor before taking payment from them and treat the guarantor similarly to the borrower. One firm out of nine responded that it did not currently comply with CONC 7 rules on arrears, default and recovery, but stated that complying with the proposed change would not lead to significant incremental impacts for them (all respondents responded 'not at all' on the impacts on their business of extending CONC 7 to guarantors). One firm suggested that it would face "slightly higher administration and postage costs" but did not quantify this. No impact on volume of lending was foreseen by firms.

4. Consumer Credit Principles. We are of the view that applying Principles 6 and 7 should not lead to significant costs for firms through requiring further changes in behaviour. All respondents to the FCA survey said that extending these Principles to guarantors would make no impact on their business.

Please provide any additional information (if required) that may assist the RPC to validate the BIT Score.

The estimates are based on a dedicated survey during the consultation stage of 18 specialist guarantor loan providers, of which nine responded, plus information from one firm that was engaging with our Supervision department on an unrelated matter. These ten guarantor loan providers originated loans totalling £154m to 53,000 customers in 2013, an estimated 80% to 90% of the market in terms of the volume of lending secured by a guarantee and includes the largest lender in the market. The smaller firms who responded to the survey confirmed that they already undertake the checks. We consider the coverage of the information gathered to be robust.

However, as with all surveys, it is possible that there may be biases in responses. In this case, as firms were not responding to the FCA anonymously, responses may have been biased by the desire to signal to the regulator that they were treating guarantors well. However, we have no other credible information base on which to assess the likely impacts of our proposals. While we acknowledge that firms may have underplayed the impact of the proposed changes, attempting to account for this in a quantitative manner is not reasonably practicable.

On the basis of the FCA survey of guarantor loan providers, in 2014 on average 11% of payments were requested from guarantors. The proportion of payments requested from guarantors but not paid was 5%.