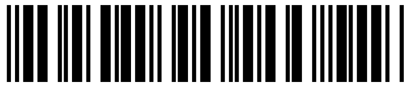
FINAL NOTICE

Unaffordable Lending Industry
United Kingdom



DATE: 23/10/2018

FINAL NOTICE

Dear Ethically Bankrupt

Despite previous correspon
outstanding on the the mo
you make contact us

FINAL NOTICE FOR THE UNAFFORDABLE LENDING INDUSTRY

WWW.DEBTHACKER.CO.UK

REPORT

DEBT
HACKER

WWW.DEBTHACKER.CO.UK

FINAL NOTICE

FINAL NOTICE FOR THE UNAFFORDABLE LENDING INDUSTRY

Wonga has collapsed. It reaped what it had sown following years of rule breaking. Others will follow.

Lenders are under explicit regulatory obligations to only provide affordable loans. Payday lenders, and other unaffordable lenders, have been ignoring those rules for years and have been piling unaffordable debts on the people who could least afford it.

Wonga, and others, are learning the hard way that borrowers have had enough and are learning about how they have been cheated. Their collapse has exposed a systemic flaw in the unaffordable lending business model; in all its forms. If customers now realise they were given a loan they could not afford then they have a strong case to get their money back, including interest, charges and even further compensation. As a consequence of other historic mis-selling scandals people are more aware of their rights to bring claims.

They have the right to bring their complaint to the Financial Ombudsman Service; and a complaint, win or lose, costs the lender £550 minimum. As this dawns on the wider public, the scale of claims will put the industry under enormous pressure:

- complaint numbers for QuickQuid have tripled since the 2nd half of 2017
- in 2018, complaints have doubled for lenders such as Lending Stream, Sunny and Payday UK

The pay day and high-cost credit industries are just the very tip of the iceberg, and they are about to be put on final notice. This will eventually reach high street lenders. Barclays, for example, received 4,633 complaints in the first 6 months of 2018 alone, many of which will include unaffordable lending.

The scale of latent unaffordable claims is enormous. “Unaffordable lending” and “over-indebtedness” are two sides of the same coin, as the unaffordable lending by regulated lenders has led to the over-indebtedness of the borrowers.

This document sets out why their historic and current unaffordable loans are going to come back to haunt them, and how people power will ensure they will.

OBJECTIVE

There are **8.3 million people** in the UK who are dangerously overindebted, and for many of them their debts have been perpetuated by unaffordable lending on a massive scale. My objective is simple, for the lending industry to change its ways. If the lending industry only provides affordable loans, as it is obliged to, then those who have been on the sharp end of irresponsible and unaffordable lending will be liberated from one of the key causes of the debt cycle that so many endure.

I will do this by putting the power in consumers hands. If consumers understand what the affordability obligations on lenders are, they will know when they have been exploited. Armed with this knowledge, they will be able to seek appropriate recourse and get back all their interest and charges. Not only that, the loan would be removed from their credit file giving many borrowers a clean slate. Understanding that affordability rules have been broken (going back years) will also aid the debt advice industry in helping overindebted people do away with the loans they should never have been sold.

In doing so they will leave the unaffordable lenders no choice. Change their ways or go the way of Wonga. Bust.

SHINING A LIGHT ON A BROKEN SYSTEM

UK families owe a **record £213.5 billion** on credit cards, car finance and short-term loans. This is because the lending system is systemically flawed, designed to create an inescapable cycle of spiralling debt by advancing unaffordable loans. This trap captures huge swathes of society, with NHS workers, teachers, and gig economy workers being the most prolific users of unaffordable payday credit.

At the heart of this problem is a simple principle that is being ignored wholesale by the industry, and unenforced by regulators. Lenders are only supposed to advance loans that are affordable. But they do not properly check whether it is affordable because, fundamentally, they just want to lend people money as that is the nature of their business, with little regard for the personal consequences for borrowers.

As someone with an extensive background in financial services, I understand the tricks of the trade and can see how the catalogue of failings have led to the current state of household finances.

However, it can be fixed and the power is in peoples' hands. My aim is simply to explain how they have been mistreated and then give them the tools to fight back.

FORCE FOR CHANGE

The payday industry is at the forefront of irresponsible lending and will be the first domino to fall. Indeed, this is already starting to happen. Wonga has fallen, and others are trying to douse the flames.

However, the flagrant disregarding of Financial Conduct Authority (FCA) rules on affordability is by no means unique to payday. Doorstep, catalogue, credit cards, car finance, and more, have a lot to answer for. The FCA obliges lenders to have a simple duty of care for their customers; and that is to check, and evidence that they checked, that the customer can afford the loan.

Credit is not a bad thing in and of itself. Credit should improve lives by allowing people to deal with life shocks or smooth the ebbs and flows of day-to-day finances. When servicing debt makes someone's life worse it is by definition unaffordable. The country's current personal debt crisis demonstrates that the billions in debt that people collectively hold was not affordable in the first place.

What is needed is a cultural change in lending behaviour and enforcement and penalties from the FCA on the already existing rules. If unaffordable lenders are suitably brought to book for unaffordable loans, then they will have no choice but to change their ways or pack their bags.

Change is coming whether the industry likes it or not as the borrowers will force that change.

Like the toxic mortgages that came to light in the 2008, **Wonga is the 'Lehman Brothers' moment for the unaffordable lending industry.** Once people understand the scale of unaffordable lending, the claims will work their way up the financial food chain. **More dominos will fall.**

However, there is danger here. The claims management industry, with an eye on the PPI deadline, sees these unaffordable loans as the next game in town – just look at Wonga. They are already starting to capitalise on what they see as a cash cow. Not only does this run the risk of vulnerable borrowers being exploited further, it also represents a clear and present danger to the ethical lending industry.

There are many ethical lenders and credit unions who do their very best to help support people. However, the very nature of their products means they are often the last resort for someone in financial distress.

Claims companies have many ethical lenders in their indiscriminate sights too, and regulators must act fast to ensure that the demise of ethical lenders does not become the unintended consequence of a consumer fightback.

INTRODUCING DEBT HACKER

DEBT HACKER

I am launching Debt Hacker, an online campaign designed to put power back in the hands of borrowers and help them fight back against exploitative high cost lending. By empowering consumers with honest information and free easy-to-use online tools, Debt Hacker will enable thousands to claim back the costs of unaffordable loans that should never have been offered to them, without targeting ethical lenders.

Debt Hacker will harness the power of social media and offer free digital support and tools to help borrowers bring an avalanche of claims and complaints. This will force the unaffordable lending industry to reform. Borrowers are fed up of being blamed for their over-indebtedness. Debt Hacker will let them know that they have a right to be protected from lenders who take advantage of them and the time has come for those rights to be exercised.

These claims through the Ombudsman are no shot in the dark. They work. Their own statistics confirm the ratio of upheld complaints:

- Wonga 72%
- QuickQuid 69%
- Sunny 65%
- Lending Stream 62%

IT'S TIME FOR PAYDAY TO PAY UP.

WE CAN NO LONGER AFFORD UNAFFORDABLE LENDING

Wonga has learnt the hard way that consumers are not powerless to fight back. Yet few consumers realise that they have rights of recourse against this pernicious industry. Few realise that if they struggled to pay a loan back (not just a payday loan) or it made their situation worse, then it was probably unaffordable and it should never have been lent to them in the first place. **In those circumstances, and there will be millions of people in those circumstances, they are owed their money back.**

Just as the banking industry learnt in 2007-8 that mortgages had been sold with little attention to their sustainability, the wider credit industry is coming to learn the extent of malpractice.

The public policy debate has focused on the country's and individuals' indebtedness. This is of course important for establishing the root causes of peoples struggles. However, the debate has failed to focus on a key protagonist in this state of indebtedness; that is the lending industry advancing unaffordable loans.

The next section details how significant elements of the credit industry have been breaking the rules, and how the people it has exploited have the power to bring it to book.

THE DEBT TRAP

Having analysed this space over a number of months and having met with many of the passionate people who support those struggling with debt, I was inspired to act after reading the House of Commons Treasury Select Committee report on Household finances: income, saving and debt (26 July 2018). Their report sets out in some detail the scale of the problem, highlighting evidence from the Money Advice Service that **8.3 million "adults in the UK – around one in six – are overindebted,** defined as being likely to find meeting monthly bills a heavy burden and/or missing more than two bill payments within a six-month period."

What's more, the Committee took evidence that the advisory services designed to help those with debt problems were overstretched to the point of "demand-suppression." StepChange, the UK's leading debt advice charity, even had to admit to the Committee that they have "been in demand-suppression mode for four years because, if we advertise, we simply cannot cope with the number of people who want our help. We have to demand-supress down to about 620,00 people a year, when we know that somewhere between 1.3 million and 1.8 million people could really do with our assistance."

The consumers who have been exploited cannot even rely on the support of the organisations who want to help them, due to the scale of the problem.

These numbers are so high because much of the lending industry has essentially been acting with reckless abandon, **lending where it was not affordable at huge scale.** Indeed their whole business model is predicated on it.

The high-cost short-term credit (HCSTC) industry, the leading offenders, spend millions on marketing to acquire its customers, a cost burden that drives more unaffordable lending to grow the loan book. They claim they charge higher rates because they lend to 'riskier customers', the fact is they charge high rates to make more profit and fuel the acquisition of more customers. It is a vicious cycle that preys on those with already precarious finances.

The biggest cost to this type of business are not the bad debts, it is customer acquisition cost. HCSTC lenders, such a Wonga and QuickQuid, report in their accounts that they expend up to 50% of operating revenues on customers acquisition costs (i.e. marketing). Therefore, by definition, the lender needs to make multiple loans once a customer is onboarded leading to unaffordable lending.

There were 10 million Payday loans annually at peak payday and over 1.4 million people use high cost credit just to keep their heads above water. Naturally, the industry has a vested interest in loaning as much as possible to as many people as possible; without caring if it is even affordable.

The FCA 2015 price cap on the payday sector just limited the amount of money lenders could make; but the business model is predicated on trapping borrowers with unaffordable lending. The industry treats the fines it receives as a mere operating cost. It did not address the core problem. These lenders should not be lending to people who cannot afford it. As Wonga has already found out, this unaffordable lending is coming back to haunt them.

The industry makes very little effort to establish whether a loan is affordable to the borrower, they instead choose to rely on paper thin credit checks as it's in their interest to do so.

The very fact that the borrower is using HCSTC, or multiple loans, should be an indication of financial distress/difficulty. It would not take much interrogation by the loan company to establish this fact. But of course they have a vested interest to forward the loan, so they do not check appropriately.

The creditworthiness checks that lenders make are inadequate. We know this because of the amount of financial distress in the market. These borrowers are after all getting the loans from lenders and not some 'magic money tree.' Lenders merely establish whether the borrower has paid debt previously, not whether they really can afford to do so. A borrower keeping on top of payments is of little significance to the reality of their circumstances in trying to keep up with those payments, whether that's skipping meals or going without other essentials. The unaffordable lending industry cares not.

WHY NOW

Our plans were already afoot when Wonga announced its deserved difficulties. Their demise simply proves that the system is broken and that people have the power to drive the worst elements of that system out of business.

The true alternative solution is a cultural change in the industry itself.

If the penalties for advancing unaffordable loans were adequate, or consumers are suitably mobilised to exercise their rights to claim against a loan that was unaffordable, the entire industry would be forced to change its practice. The costs of advancing unaffordable loans would now sit squarely with the lender, with the borrower entitled to recover all interest and charges (plus interest).

They can and should act differently. For there is ample opportunity to lend differently; and modern technology and new Open Banking rules make it entirely possible to make appropriate affordability checks. There has also been extensive work in the field on how affordability can be appropriately assessed. In short, the industry has run out of excuses.

ENFORCE THE EXISTING RULES

A root cause identified by the Treasury Committee is that borrowers have little financial resilience and were therefore very susceptible to "life shocks", forcing them into the arms of high-cost credit, multiple loans, overdrafts and huge credit card debts.

The Committee's insights into the causes of indebtedness are a valuable intervention in the debate. However, I was shocked that at no point in their wide-ranging report was the specific issue of the lenders responsibility explicitly addressed. Namely that it is incumbent on the lender to provide affordable loans, where they have not they have broken the rules.

The lenders responsibilities are the key linchpin that is being missed by lawmakers, policymakers and regulators.

UK Finance is a trade association representing 300 of the leading lenders. In its written submission to the Committee it notes that a customer's circumstances can change, and the potential for future changes should be factored as part of the affordability assessment.

However, in the very same submission UK Finance then claimed the 8.3 million over indebted arose entirely from unforeseen changes in circumstances. This is a risible way of deflecting responsibility.

THE EXISTING RULES

The rules are quite explicit. The FCA consumer credit handbook sets out a firm's responsibility as follows:

1. (a) the potential for the commitments under the regulated credit agreement to adversely impact the customer's financial situation, taking into account the information of which the firm is aware at the time the regulated credit agreement is to be made[2]

In plain English, is the loan affordable, i.e. the loan should not have made the borrower's position worse. In assessing that, the FCA say the lender is supposed to consider the following:

1. the type of credit;
2. the amount of the credit;
3. the cost of the credit;
4. the financial position of the customer at the time of seeking the credit;
5. the customer's credit history, including any indications that the customer is experiencing or has experienced financial difficulties;
6. the customer's existing financial commitments including any repayments due in respect of other credit agreements, consumer hire agreements, regulated mortgage contracts, payments for rent, council tax, electricity, gas, telecommunications, water and other major outgoings known to the firm;
7. any future financial commitments of the customer;
8. any future changes in circumstances which could be reasonably expected to have a significant financial adverse impact on the customer;
9. the vulnerability of the customer, in particular where the firm understands the customer has some form of mental capacity limitation or reasonably suspects this to be so because the customer displays indications of some form of mental capacity limitation.[1]

The above boils down to a few key checks the lender should be making:

- The loan should not make the borrower's financial position worse
- It should take account of the customer's income, having accounted for essential expenditure and existing loan repayments, i.e. if the repayments are more than what is left then it is clearly not affordable
- If the customer has to sacrifice paying a utility bill, paying their rent, food, etc, in order to pay the loan then it is clearly not affordable

In assessing the responsible steps that a lender should take we must ask the following:

- Income – how carefully did they check and use this information before providing the loan?
- Expenditure – how carefully did the lender check this?
- Existing credit agreements – how carefully did the lender take this into account before issuing the loan?
- Did the lender calculate that the customer's income, having accounted for essential expenditure and already committed credit repayments, to ensure that the loan repayments were affordable?

WHERE THIS HAS NOT HAPPENED, LIKELY THE MAJORITY OF CASES, AND THE BORROWER HAS STRUGGLED WITH THE LOAN, THEN THE LOAN WAS NOT AFFORDABLE.

[1] CONC 5.2 Creditworthiness assessment: before agreement https://www.handbook.fca.org.uk/handbook/CONC/5/2.html

MOBILISING PEOPLE POWER

The problem is that not enough consumers, or even some of the support network for debt advice, realise that lenders are under these sorts of obligations. Neither do they realise that the simple act of keeping up with repayments does not constitute affordability. If they struggled to pay it back, they probably could not afford it.

Armed with the knowledge of what they should and should not have been lent, and clear direction on how to bring a claim against a lender who has broken the rules, people can change the system.

Debt Hacker, a not for profit campaign, will arm them with that knowledge and give them the tools to bring claims against lenders, clearly, simply, and free of charge.

A successful claim through the Financial Ombudsman Service (FOS) can get the borrower back the entire interest and charges on a loan they paid off; or the interest and charges on an outstanding loan with the remainder settled in affordable payments. Furthermore, a claim brought to FOS costs the lender £550 win or lose. Lenders are not allowed to discriminate against the borrower and the claim is not recorded on their credit file or score. It is incumbent on the lender to prove they made appropriate checks on the loan's affordability. We know many have not been taking such steps.

It costs the borrower nothing to make a claim, and it costs the lender £550 minimum. When the millions of consumers who have been mistreated realise the power is in their hands, and Debt Hacker puts the right tools in their hands, the bad loans of the past and the present will catch up with them quickly.

Yet this avenue for recourse carries with it an inherent danger. Claims management companies are already targeting the lending industry indiscriminately.

Many ethical lenders, who are often the lender of last resort for those in financial distress, are becoming the first in the firing line for claims companies. Invariably, being social enterprises or charities, their balance sheets cannot withstand these indiscriminate and sometimes spurious claims. Regulators must act to prevent ethical lenders becoming the collateral damage of industry change.

For the scale of claims is potentially enormous. The FCA have already cost the industry £1bn through fines and loan write offs for inappropriate lending, but the vast majority of consumers have seen little pay back for being burdened with unaffordable lending. Their mis-selling goes back up to six years to the heights of the payday lending industry, before the price caps came into effect. There are literally millions of loans that will come back to haunt them, not to mention the unaffordable loans that continue to be advanced today.

BRINGING THE INDUSTRY TO BOOK

Let us take a practical example. In recent years Provident Financial Home Credit has been making 32% return on assets, with peaks of 40% in the last decade. This is staggering when you compare it with Apple, the most profitable company in the world at 27% profit in its most recent accounts.

To achieve as much as 40% return on the backs of struggling people, when the banking sector as a whole struggles to make over 5%, illustrates that Provident's financial model is predicated on unaffordable lending.

If Provident are called to account for their unaffordable lending by the people who have been exploited, they will be left with a choice. Start lending affordably or go out of business.

When the overwhelming cost of historic bad practice threatens the entire industry, and lenders very existence, then market forces will dictate changes in lender behaviour – just as it did with mortgages post-2008. That is why Wonga is the 'Lehman Brothers' moment for the entire industry.

The domino effect has started with the payday loan industry as they are often the loan of last resort. Yet customers will quickly realise that there were other loans before they had to resort to payday that put them in that position in the first place; and were therefore unaffordable too.

Lenders affordability failures now represents a contingent liability for historic and current unaffordable loans.

This is a financial 'asbestosis' stretching from the present back years, covering millions upon millions of unaffordable loans. A terrifying level of contingent financial risk arising from burdening borrowers year in year out with unaffordable loans.

By slowly working back through their loan portfolio, with the assistance of the Ombudsman, millions of citizens will eventually get to a stable basis where the only loans remaining are only the affordable loans.

MAKE THEM RESPONSIBLE

The boards of those unaffordable lenders will be under a personal obligation to assess the risk of exposure they have to these bad loans, provide for it on their balance sheets, and disclose it to their shareholders and contingent claimants in their financial statements.

This in turn will inform and encourage borrowers to claim as the industry publicly acknowledges the financial scale of their historic failings – as people will literally be able to see how much the lenders think they owe. As with other historic mis-selling scandals, such as PPI, the cost will begin to balloon.

Should there be insufficient provisions to meet these liabilities the board of directors of these lenders will be personally responsible should they be found to have wrongfully traded those companies.

Cultural change in lenders will be expedited when there is a clear and present danger to the leadership's personal balance sheets.

THE COURSE OF EVENTS

AS THIS REALISATION DAWNS ON THE UNAFFORDABLE LENDERS, EXPECT TO SEE THE FOLLOWING UNFOLD:

- The number of claims led by Debt Hacker and others begin to mount
- The lenders will ask the FCA to protect them
- As the numbers start hitting profit targets and budgets, the lenders will carry out an initial assessment of the risk
- They will cling to the hope that the public are not motivated enough to claim at scale
- The FCA will examine the situation as the claims grow and more lenders fall into difficulty
- If the lender is a public company they need to disclose it as one of the emerging risks of the business in their financial statement by making a provision for the liability. The FCA and auditors will assess the basis of the provision
- The management and board will start in fighting and heads will roll
- They change the unaffordable underwriting policies and start making better (though not proper) assessments on affordability, claiming the problem has been fixed
- Lending and profitability falls just when they need those profits to meet increasing levels of claims
- New management and boards will come in, overseen by the FCA, and make an assessment of the liability and advise shareholders
- The lenders bankrollers will start to pull out of these markets putting greater stress on the balance sheets
- The directors will now have to consider their personal liabilities in the event of a lender's insolvency
- They appeal to the FCA for assistance, who will no doubt show them as much consideration as the lenders showed their customers in their history of unaffordable lending
- To protect the board from the risk of wrongfully trading they seek the advice of external lawyers, accountants and bankers
- The claims continue to grow, they fail to meet the statutory deadline for dealing with the claims; they become overwhelmed (as was the case with Wonga)
- The independent lawyers and accountants carry out strategic reviews with a full assessment of the liabilities
- The lenders go back to their shareholders for support – they get none
- Lenders who do not change or cannot meet their liabilities go under
- For those that do not survive, and where the liquidator can make a claim for wrongful trading, the liquidator is obliged under statue to pursue each and every director involved in those companies against their personal balance sheet for a recovery for the unsecured creditors.

CHANGE

- Those who have survived or are new entrants in the market are now, no doubt, ensuring their loans are affordable
- People are getting a fair deal.

DEBT HACKER

Alan Campbell

WWW.DEBTHACKER.CO.UK