August 2014

payday lending: pieces of the picture

Financial Ombudsman Service insight report

This report was prepared by Mike Harris, head of policy insight, and Jo Thornhill, policy insight manager, in collaboration with the ombudsmen and adjudicators of the ombudsman service's consumer credit team, and with support from the ombudsman's policy, business information and communications teams.

foreword

The ombudsman received 794 complaints about payday loans last year, an increase of 46% on the previous year. Despite the increase, we are very concerned that the number of payday loan complaints we see does not reflect the level of public concern about these products. We decided to take a closer look at the complaints we do receive to get a better understanding of what is going wrong and to see what lessons might be learned and shared.

What we have seen is quite distressing. Some of the problems consumers have encountered will be familiar following the intense media scrutiny of payday lending over the last couple of years – unhappiness with the high cost of credit, unfair or multiple charges, and the excessive use of continuous payment authorities to take money from customers' accounts, sometimes leaving them unable to pay for food or their bills. The Financial Conduct Authority has acted in recent months to address these issues. We will report on any systemic breaches of the new rules that we see.

> "Our review uncovered good, satisfactory and – at the extreme end – some appalling treatment of borrowers in difficulty."
>
> **Caroline Wayman, chief ombudsman**

Running through many of the complaints we reviewed was repeated evidence of poor administration and lenders displaying inadequate customer care towards those struggling financially. While we have seen some examples of lenders doing the right thing for consumers in very difficult circumstances, in too many cases the treatment of consumers was alarming. Our review uncovered a very mixed picture of good, bad and – at the extreme end – appalling treatment of borrowers in financial difficulty. We heard from many vulnerable consumers who had been unable to set up a repayment plan with their lender, or who had been aggressively chased for debt. This is completely unacceptable – industry practice in this area simply has to improve.

We will not hesitate to refer to the regulator those businesses that ignore their obligations. But we will also work with the industry to help embed good practice as well as report bad.

We are firm believers that complaints are a great barometer for how any business is performing, and that the opportunity to learn from customers who are dissatisfied can help prevent things that have gone wrong in the past from going wrong again in the future.

As a service, we are determined to play a full and active role in that effort. Looking ahead, I am determined that the ombudsman service seeks new ways to share the insight we gain from the hundreds of thousands of financial services complaints we tackle each year. This report is the first step in that continuing drive. I hope you find it useful and informative.

Caroline Wayman, chief ombudsman and chief executive

contents

"settling disputes, without taking sides … "

"… using our insight to help prevent future problems."

The Financial Ombudsman Service was set up by law to resolve individual disputes between consumers and financial businesses – fairly, reasonably, quickly and informally.

We can look at complaints about a wide range of financial and money matters – from insurance and mortgages to investments and credit.

If a business cannot resolve a consumer's complaint, we can step in to settle the dispute. We are independent and impartial. When we decide a complaint we look carefully at both sides of the story and weigh up all the facts.

If we decide a business has treated a consumer fairly, we will explain why. But if we decide the business has acted wrongly – and the consumer has lost out – we can order matters to be put right.

We are constantly looking for ways to improve the way we resolve cases, and we aim for the highest professional standards.

We believe it is essential to learn lessons from dissatisfaction and disputes. So we have an important role in sharing the insights that can be gained from the complaints we see. This gives consumers greater confidence in financial services and helps businesses prevent future problems by learning from situations where things have gone wrong.

chapter 1

introduction and executive summary

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background

Payday lending has grown rapidly in recent years, but the first UK payday lenders have been around for more than a decade. Expansion has been fuelled by payday lenders from the United States looking to new markets and countries for opportunities in response to tightened domestic regulation, and also by diversification by UK lenders offering other types of credit product.[1]

According to the Competition and Markets Authority (CMA), growth in the payday lending sector was particularly strong between 2010 and 2012.[2] In 2013, it is estimated that payday lenders issued more than 10 million loans, to 1.6 million payday loan customers, with a total value of £2.5 billion.[3]

Clearly, the growth in supply is only one side of the story; payday loan businesses could only flourish if there was demand. UK consumers are heavily indebted.[4] Recent research suggests that almost half the population are now suffering some form of financial insecurity.[5] Payday lending has filled a gap in the market, particularly for those consumers with a poor credit history who are excluded from mainstream credit.

At the point of applying for a high-cost short-term loan, many consumers are in a difficult, and deteriorating, financial situation.[6] As one ombudsman put it during our research, for many, taking out a payday loan is in itself a 'distress purchase'.

scrutiny

Payday lending has consequently become increasingly controversial, attracting significant media, political and regulatory attention. Consumer groups, debt advice charities and others have been expressing concern for many years about the payday lending business model, the high cost of credit, poor business practice and lenders' treatment of consumers in difficulty.

> "some 5 million people in this country use payday loans. The situation is becoming too big to ignore."
>
> **Justin Welby, Archbishop of Canterbury House of Lords, 20 June 2013**

In June 2010 the Office of Fair Trading (OFT), the former regulator of consumer credit, published a report on high-cost credit and found significant failings. A further OFT report published in March 2013 found widespread non-compliance with the Consumer Credit Act and voluntary codes of conduct by businesses. By June 2013, the OFT had referred the industry to the Competition Commission (now the CMA), which published provisional findings in June 2014 and made numerous recommendations to improve competition in the sector. Parliamentary scrutiny has come in the form of an investigation by the Business, Innovation and Skills Select Committee, whose December 2013 report made calls for more rigorous affordability checks, a cap on 'rollovers' (when a loan is deferred)[7] and health warnings to appear on advertising.

The Financial Conduct Authority (FCA) assumed responsibility for consumer credit regulation from 1 April 2014, and quickly introduced new rules to address issues of particular public concern, including limiting the number of times payday loans can be rolled over, and the number of times lenders may unsuccessfully use a 'continuous payment authority' (CPA).[8]

The regulator is currently conducting a thematic review of the payday lending market, which will examine how lenders collect debts and manage borrowers in arrears. During its investigations into the sector, the FCA has found that:

"... *excessive charges for high-cost short-term credit are harming significant numbers of consumers. Many borrowers pay a high price for a loan that is of limited net benefit, or makes their already difficult financial situation worse. Borrowers who have problems repaying can end up owing significantly more than they originally borrowed.*"[9]

> "what we are concerned about are the people who frankly shouldn't be lent to, who can't afford the loans and who then get rolled over and get pushed ever further into a debt cycle."
>
> **Martin Wheatley, Chief Executive, Financial Conduct Authority**
> **BBC 5Live, 1 April 2014**

In July 2014 the FCA published a consultation paper on capping the total cost of credit. The proposal is for a cap which will apply to all interest, fees and charges associated with high-cost short-term loans, and to prevent consumers being charged more than 100% of the original loan amount. The regulator estimates that the cap will benefit consumers in the form of lower prices, and reduce firms' revenues by 42% (approximately £420 million).[10] The cap will come into effect from 2 January 2015.

complaints

Against this backdrop of increased scrutiny, the number of consumers bringing complaints about payday loans to the Financial Ombudsman Service has been rising year on year. As chapter 2 sets out in more detail, the number of new payday loan cases opened by the ombudsman service increased by 168% between March 2012 and March 2014 (from 296 complaints to 794). But despite this proportionately steep increase, 794 remains a relatively low number in the context of our total casework volume. We do not believe our payday loan complaints caseload necessarily reflects the scale of consumer detriment in this market.

The payday loan market is set for rapid and significant change. The new regulatory regime and the forthcoming price cap are expected to result in a number of current lenders leaving the market.[11] Others will look to innovate or diversify into other product areas. The instability of the sector, the strengthening of regulatory oversight, and the continued growth in complaints, has prompted us to look in more detail at the payday cases we decide.

The ombudsman service often sees the hardest-fought disputes, which financial businesses and consumers have already tried and failed to resolve themselves. Because we sit 'downstream' of where problems occur, our report is not, cannot, and does not pretend to be, a commentary on or analysis of the wider high-cost short-term credit industry. But by looking in detail at the complaints consumers have brought to us, we hope our insight will complement what others have observed, help payday lending businesses understand more about the causes of consumer detriment in this market, and support effective regulation. We also anticipate that our findings will be of interest to policymakers, consumer groups and the wide range of organisations supporting consumers with debt or money problems.

executive summary

This report presents the findings from the payday loan complaints we have reviewed. It is the first in a new series of insight reports from the Financial Ombudsman Service, and brings together our statistical data on the payday lending complaints we receive, a detailed look at a sample of complaints received in the 2013/14 financial year, and qualitative interviews with ombudsmen and adjudicators involved in resolving payday cases. Our findings are summarised below.

payday loan complaints handled by the ombudsman service in 2013/14

The ombudsman service opened **794 complaints** from consumers about payday lending in the 2013/14 financial year, a **46% increase** on the previous year (542 complaints). Of the complaints we resolved during the year, we **upheld 63%** in favour of the consumer. In addition to the formal complaints we handle, the ombudsman also continues to receive a growing number of enquiries from consumers about payday loans. In 2013/14, the ombudsman service's customer contact division (CCD) fielded **5,277 payday loan-related enquiries** from consumers.

the sample of complaints we looked at in our research

To deepen our understanding of the issues underpinning the payday lending complaints we receive, we looked in detail at a sample of **353 complaints** that had been both opened and closed in 2013/14. The sample included complaints against **46 different businesses**. The age, gender and region of the consumers represented in the sample closely matched the overall profile of those complaining to the ombudsman about payday loans in 2013/14. Many of the consumers in the sample had taken out previous payday loans, and there was evidence that over two-fifths **(42%) were in financial hardship**. Where it was possible to determine the date of the loans at the centre of the sampled complaints, 72% were taken out between 2012 and 2014.

why consumers had complained about payday loans

As expected, consumers' reasons for bringing complaints to the ombudsman service were **complex and varied**. There was no single, dominant reason for consumer complaints. Rather, we found complaints to be **multi-faceted**, often featuring a combination of reasons for complaint. The leading *main* reasons for complaint were **allegations of fraud, poor administration, the unauthorised or unexpected taking of funds, and the inability to agree a debt repayment plan** with a lender.

Taking *all* observable features of complaints into account, the most frequently-cited issues were **damage to credit records, poor customer service and poor administration**.

complaints about fraud

In just over one in six (16%) of the sampled cases the complaint was about a loan the consumer said they had not taken out. The headline result covers a **varied range of issues** and circumstances, from alleged identity theft and scams to fraud perpetrated by someone known to the consumer. While all age groups can be vulnerable, we found that **younger consumers were more likely to complain about fraud** than older consumers: fraud was the main reason for complaint for 39% of those aged 18-24, compared to 15% among the over-55s.

complaints about damage to credit records

12% of the sampled cases featured damage to credit files as the principal reason for complaint. In all, complaints about damage to credit files featured – to some extent – in a **quarter (24%) of the sampled cases**. Our review revealed widespread consumer concern about the condition of their credit files, but also **a lack of detailed understanding** about how credit reference agencies and personal credit files work. Some consumers in our sample had deliberately taken out a payday loan to improve their credit score, and complained that they had been misled.

complaints about debt-chasing, poor administration and customer service

We saw considerable evidence of consumers encountering **problems agreeing a debt repayment plan** with their lender, or expressing unhappiness at what they felt to be **insensitive debt collection practices**. These issues were often interlinked. Complaints about **poor administration** by lenders – such as loans paid into the wrong account or the miscalculation or misapplication of fees and charges – also featured prominently in our research. **Poor customer service** was a thread running through many of the cases reviewed, often serving to exacerbate the effect of other issues.

complaints about continuous payment authorities (CPAs)

The **unexpected or unauthorised taking of funds** from an account (via a continuous payment authority) was the third most common main reason for consumers in our sample to bring a complaint to the ombudsman. More than one in ten of the cases we reviewed (13%) featured the alleged misuse of a CPA as the main reason for complaint. It was also a subsidiary issue in other cases: when all features of complaints were considered, unhappiness about the use of CPAs were observable in a fifth (19%) of cases.

complaints about high costs and charges

At the start of the review, we anticipated to find the high cost of credit to be a prominent driver of consumer complaints. Our findings were surprising: in just 4% of the sampled cases were high interest rates cited as the main reason for complaint. High charges were the main reason in 3% of the sample. But this is only part of the picture – **the cost of credit emerged as a background feature in a much higher proportion of reviewed complaints**. We also found vulnerable consumers, including those in financial hardship, to be more likely to complain about high charges and interest.

the experience of vulnerable consumers

A significant proportion of complaints featured consumers in obvious **financial hardship**, struggling to repay their debt. In all, over half of the sample featured what might be considered an indicator of possible vulnerability, including financial distress, unemployment, disability, long-term illness and mental health issues. Vulnerable consumers were **more likely to have rolled over and topped up** their loans, and were more likely to have loan debts outstanding at the point they brought their complaint to the ombudsman. Businesses' treatment of vulnerable consumers varied. We saw **evidence of both good and bad practice**. Where bad practice did occur, however, it often caused a rapid escalation of the consumer's debt problem.

payday lenders' signposting of consumers' referral rights

If a financial business cannot resolve a consumer's complaint by the end of the next business day, it must respond within eight weeks, writing to the consumer to inform them of its decision. The 'final response letter' must explain that the consumer has the right, if they are unhappy with the decision, to refer their complaint to the ombudsman service. In just under half of the sampled cases, consumers were given full referral rights. In the remaining cases, however, there was a **mixed picture of practice**. In some cases, referral rights had not been given at all, were incomplete, misleading or late. In a significant proportion, a final response letter was not issued at all. We are **extremely concerned** that too many consumers are not being informed of their right to have their complaint independently reviewed.

live issues

The payday loan industry is a dynamic and fast-paced market, with practice evolving against a backdrop of tightened regulation and considerable public scrutiny. Having completed our review of a sample of complaints received in the last financial year, we conducted follow-up interviews with ombudsmen and adjudicators working on the most recent cases to take account of emerging issues. Those interviewed said the apparent **unaffordability of payday loans** at the point of sale was a growing cause of concern. We are seeing a big increase in the number of enquiries from consumers about problems with **credit broking services**. Ombudsmen and adjudicators also reported a shift in emphasis away from the 'traditional' 30-day payday model towards **new loan products**.

conclusions

Our review of payday lending complaints found many recurring and interlinked themes. More needs to be done to improve public understanding of **how credit systems operate,** though this is an issue that extends well beyond payday lending. The complaints we reviewed revealed repeated evidence of lenders displaying **sloppy administration** or demonstrating little concern for **customer care**. This simply isn't acceptable. Our review also gives us cause for concern about the **treatment of borrowers in financial difficulty**, too many of whom were treated unsympathetically.

We remain extremely concerned by the quality of businesses' **final response letters**, and the patchy way in which some lenders provided consumers with appropriate referral rights to the ombudsman. There must be no unnecessary barriers between consumers and their entitlement to have complaints independently reviewed.

what can businesses do?

- **End poor administration.** Lenders should not be causing their customers undue trouble and upset because of poor systems and process. Putting resources into improving this area should reap rewards in customer satisfaction.
- **Make customers central to the business.** If a customer feels the need to raise an issue with a business, the business can often stop dissatisfaction escalating by listening and trying to put things right early.
- **Make sure consumers know their rights.** Full 'referral rights' are still not being provided consistently. The ombudsman service is working with businesses to raise standards in final response letters and will continue to flag poor practice to the FCA.
- **Help vulnerable consumers.** Some consumers find themselves in considerable financial difficulty. It is in everyone's interest to work together to find solutions, such as setting up viable debt repayment plans, rather than ignoring the problem and continuing to chase for debt.
- **Work with credit reference agencies to ensure that consumers' credit files are accessible, transparent and easy to understand.** More needs to be done by industry and credit reference agencies to improve clarity and build consumers' understanding in this area. It is particularly important for those who have experienced impaired credit in the past.

consumers can make things better by:

- **Seeking debt help early.** It is easy for debts to spiral out of control quickly. Consumers who experience problems with their loan should make their lender aware as soon as possible. Lenders can freeze interest and charges and set up a reasonable repayment plan. Consumers can speak to their bank as well as creditors – the bank can cancel a CPA, for example.
- **Not being afraid or ashamed to complain.** The ombudsman service is here to help and can guide people through the process.
- **Getting free and independent debt advice.** Debt advice charities, such as StepChange, can help, or get in touch with the ombudsman. We can guide consumers towards those who can help them get on top of debt problems for free. The Money Advice Service also has information and advice to help consumers get their finances back on track.

chapter 2

the payday lending enquiries and complaints we received in 2013/14

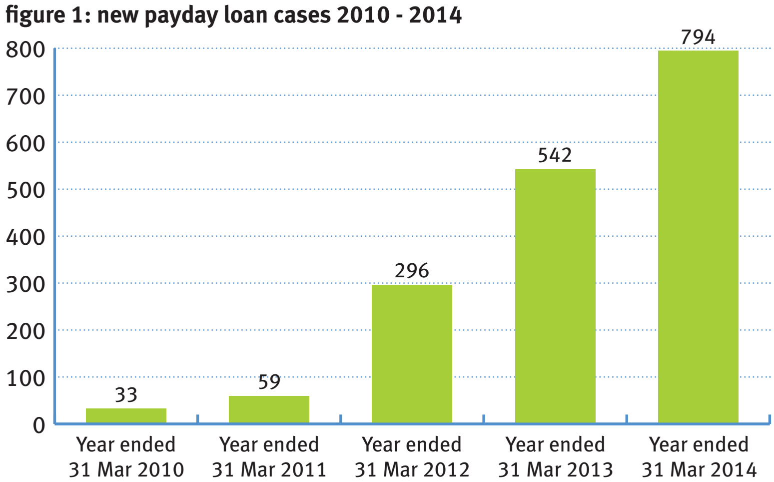
2 the payday lending enquiries and complaints we received in 2013/14

This chapter details the number of enquiries and complaints about payday lending handled by the ombudsman service in the financial year 2013/14, the profile of those consumers who contacted us, and how the volume of enquiries and complaints has grown over recent years.

snapshot

- The ombudsman service opened 794 consumer complaints about payday lending in the 2013/14 financial year, a 46% increase on 2012/13 (542 complaints). In total, we resolved 660 payday lending complaints, upholding 63%.
- 60% of payday loan complaints were brought by men, and 39% by women.
- Payday loan complaints were most likely to be brought by consumers aged under 35 (47%) and by consumers based in London (18%).
- While the number of payday loan complaints remains small relative to the ombudsman service's overall caseload (we received a total of 512,167 new complaints in 2013/14), we have been receiving a growing number of enquiries from consumers to our helpline.
- Since January 2009, we have received 12,084 enquiries about payday lending from consumers, with 5,277 (44%) of these coming in the last financial year alone.

figure 1: new payday loan cases 2010 - 2014



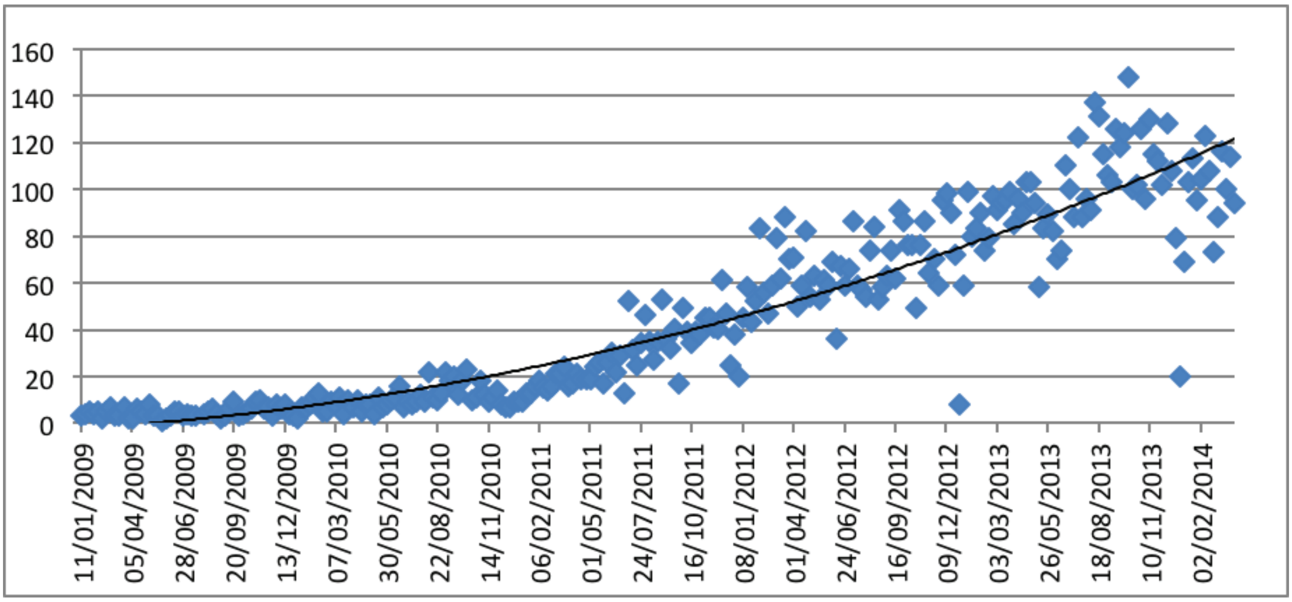
sources: Financial Ombudsman Service, *Annual Review 2012/13*, and *Annual Review 2013/14*; and Office of Fair Trading, *Payday Lending Compliance Review. Final Report*, March 2013, p. 26.

consumer complaints about payday lending in 2013/14

The ombudsman service opened 794 new payday loan complaints in the last financial year, a sharp increase (46%) on 2012/13, as figure 1 shows. The number of consumers complaining to the ombudsman about aspects of payday lending appears to be on a clear upward trajectory, albeit from a low base.

> "There is a significant mismatch between what debt charities say they are seeing, and the economic period we have just been through, and what we at the ombudsman are seeing on our front line. We are not seeing the volumes of payday loan complaints we would expect, given the implied size of the problem."
>
> **Juliana Francis, senior ombudsman**

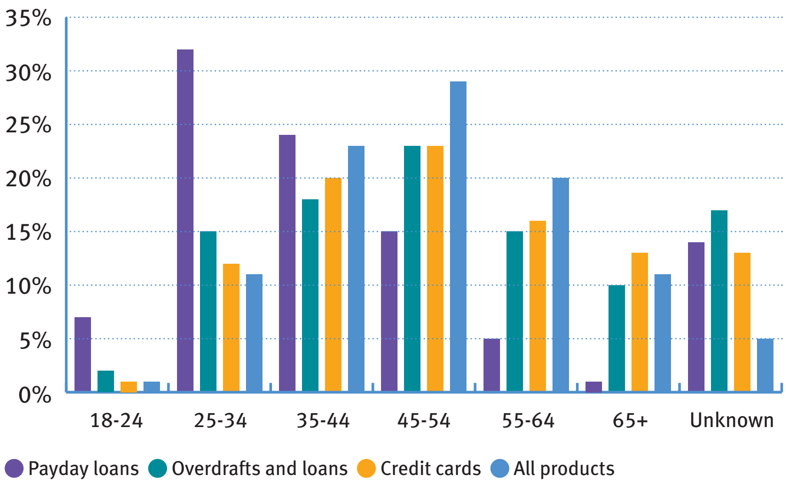
figure 2: payday loan enquiries by week, January 2009 to March 2014



Despite the number of complaints having more than doubled over the last two years, we are not convinced that our payday loan caseload necessarily reflects the actual scale of consumer detriment in this area. We get a sense of this from the calls we receive from consumers that don't necessarily crystallise into formal complaints. The ombudsman's customer contact division (CCD) is our initial contact point for consumers. The frontline advisers on our helpline deal with all initial enquiries and complaints, giving general advice and guidance to consumers on what to do if they have a complaint about a financial product or service. In total, we handled over two million initial enquiries and complaints last year.[12]

The number of weekly enquiries to the ombudsman about payday loans has been growing steadily in recent years, as figure 2 shows. In the financial year 2013/14, we received 5,277 enquiries from consumers about payday lending.

figure 3: age profile of consumers bringing complaints to the ombudsman service, financial year 2013/14



source: Financial Ombudsman Service.

the consumers who brought complaints to us

The consumers who brought a complaint about payday loans to us in the last financial year were considerably more likely to be drawn from younger age groups than those complaining about other financial products.

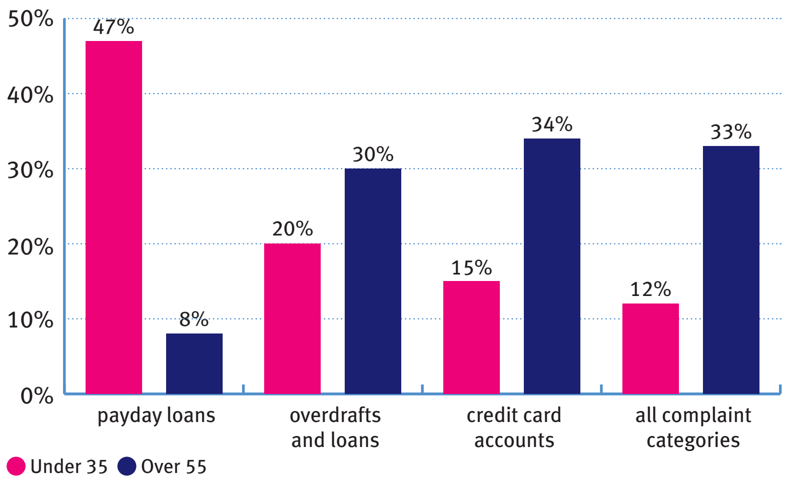
As figure 3 shows, there was a particular spike in the 25-35 age bracket when compared to other types of financial complaint, including complaints about other consumer credit products such as overdrafts and credit cards.

This bias towards younger consumers is not a surprising finding in the context of the payday lending market research undertaken by the former Competition Commission (now the Competition and Markets Authority), which showed that payday loan customers are typically younger than the UK population as a whole.[13] The scale of the contrast in age profile of consumers complaining about payday loans compared to other financial products is underlined in figure 4, which compares the respective proportions of consumers aged below 35 and above 55 across selected product categories.

While we found that the age profile of consumers bringing complaints to the ombudsman service about payday lending was markedly different to complaints about other types of product, the geographical distribution of consumers was very similar. Figure 5 shows the regions accounting for the highest proportions of payday complaints were London (18%), the South East (11%) and the North West (11%).

The former Competition Commission's research into the payday lending market found that the regional distribution of payday lending customers broadly reflected the distribution of the UK population.[14] It found that payday lending customers were slightly more concentrated in London relative to the population, but that the differences were small.

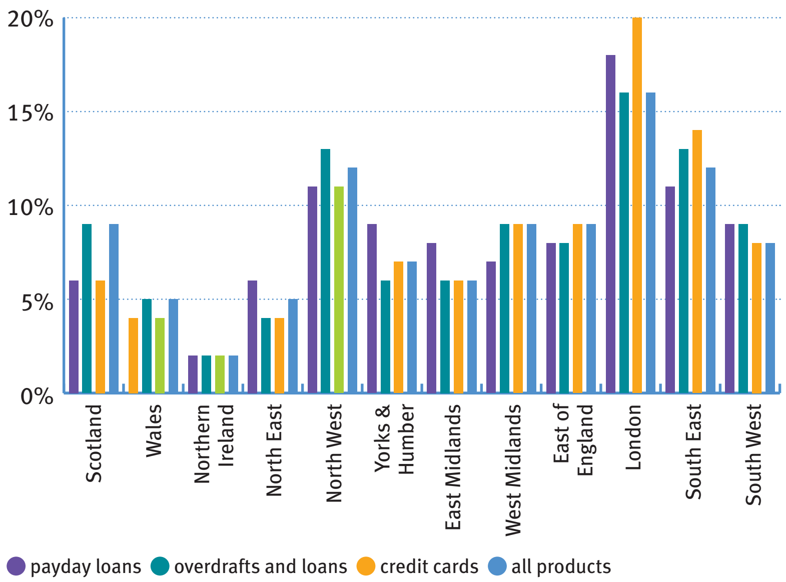
figure 4: proportion of consumers aged below 35, and above 55, in 2013/14 – payday loan complaints compared to other complaint categories



source: Financial Ombudsman Service. Chart excludes complaints where the consumer's age was unknown.

This pattern is echoed in our own distribution data. Figure 6 overlays the geographical region of consumers complaining to the ombudsman service about payday loans with the Competition Commission's market data and the UK's population distribution. It shows that consumers in London accounted for a higher proportion of ombudsman complaints (18%) than the wider payday market (16%) or UK population distribution (13%). We also saw a slight overrepresentation in complaints from Yorkshire and Humberside (9%) compared to the market data (6%). The reverse picture applied in the South East (11% against 15%), the East of England (8% against 11%), and the West Midlands (7% against 10%).

figure 5: regional distribution of consumers bringing complaints to the ombudsman service, financial year 2013/14

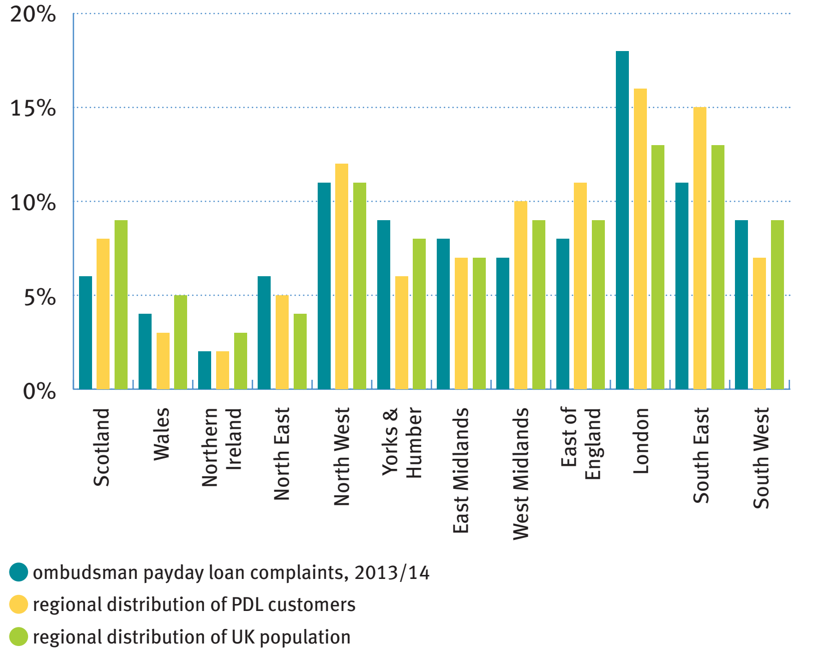


source: Financial Ombudsman Service.

the businesses consumers complained about

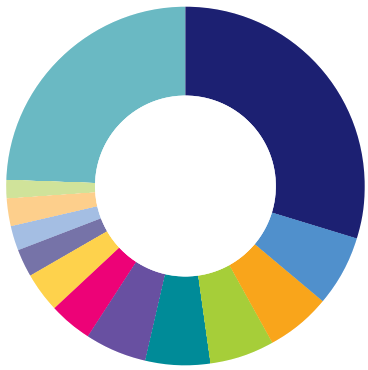
The businesses accounting for the largest number of complaints about payday lending are shown in figure 7. For the purposes of our statistical reporting, complaints to the ombudsman service are categorised according to group name, which will often be less recognisable than the businesses' various trading names shown in table 1. For example, WDFC UK Limited, against which we received 237 new complaints in 2013/14, is better known by its trading name Wonga.com.[15]

figure 6: Regional distribution of payday loan customers compared



sources: Financial Ombudsman Service; and Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014.

figure 7: converted cases by business, 1 April 2013 to 31 March 2014



WDFC UK Limited	**237**
Casheuronet UK LLC	**50**
Cfo Lending Limited	**47**
Express Finance (Bromley) Limited	**47**
Microcredit Limited	**46**
MEM Consumer Finance Limited	**43**
Instant Cash Loans Limited	**32**
Lending Stream Limited	**28**
Web Loan Processing Limited	**20**
Ariste Holding Limited	**19**
PDL Finance Limited	**18**
Motormile Finance UK Limited	**15**
other	**192**

source: Financial Ombudsman Service.

table 1: business groups and their trading names

business group name	example business trading names include...
WDFC UK Limited	Wonga.com
Casheuronet UK LLC	Quick Quid; Pounds to Pocket; Web Cash Loans
Cfo Lending Limited	Payday First; Payday Advanced; Cfoloans.com
Express Finance (Bromley) Limited	Payday Express; Wage Advance; Fast Forward Loans
Microcredit Limited	Minicashloans.Co.Uk; MiniCredit.co.uk
MEM Consumer Finance Limited	Payday UK; Payday Now; The Payday Store
Instant Cash Loans Limited	Money Shop; Cash Centres
Lending Stream Limited	Payday Loan Store; Smartphone Loans; Check2Cash
Web Loan Processing Limited	Cashkingdom; Fastloanforyou; Toothfairy Finance
Ariste Holding Limited	Cash Genie; Go Cash
PDL Finance Limited	Mr Lender

source: Financial Ombudsman Service.

the complaints we resolved

Overall, the ombudsman service resolved 660 consumer complaints about payday loans in the last financial year, upholding 418 (63%). The service works hard to ensure that, wherever possible, the delays caused by the high volume of Payment Protection Insurance (PPI) cases we receive do not adversely affect our handling of cases involving other financial products. In the last financial year we resolved 51% of payday loan complaints within three months and 80% within six months.[16] We are also currently piloting new approaches to handling the enquiries consumers bring us about payday loans, to ensure that we provide help as quickly as possible.

The ombudsman service records the outcome of a consumer's complaint as "upheld" where:

- The financial business told the consumer in its final response that it had done nothing wrong but after the complaint was referred to us, we decided (or the business belatedly accepted) that it had done something wrong after all; *or*
- The financial business's final response offered the consumer inadequate compensation but after the complaint was referred to us, we required the business (or it belatedly agreed) to increase its offer to an appropriate level.

table 2: proportion of consumers' complaints upheld by the ombudsman service in 2013/14, by business group

business (group)	number of resolved complaints	number of complaints upheld	proportion of complaints upheld
WDFC UK Limited	157	93	**59%**
Microcredit Limited	53	41	**77%**
Express Finance (Bromley) Limited	48	29	**60%**
Casheuronet UK LLC	37	26	**70%**
Cfo Lending Limited	35	27	**77%**
Instant Cash Loans Limited	33	15	**45%**
MEM Consumer Finance Limited	29	15	**52%**
Lending Stream Limited	25	20	**80%**

source: Financial Ombudsman Service.
Table includes businesses with at least 20 resolved complaints.

We record the outcome of a complaint as "not upheld" in cases where:

- The financial business had done nothing wrong; or
- The financial business had done something wrong, but had already offered the consumer appropriate redress (before the complaint was referred to us).

It is worth noting that just because we don't uphold a complaint on its merits does not mean that the consumer might not feel upset and let down by the way the business has treated them. Similarly, the fact that a consumer hasn't found the perfect words to express their complaint does not automatically mean that a case has no merit. Individual uphold rates can be affected by a number of factors but generally a high uphold rate is cause for concern.

As table 2 illustrates, uphold rates can vary considerably by business. For example, the ombudsman service upheld 80% of payday loan complaints against Lending Stream Limited in 2013/14, 59% of complaints against WDFC UK Limited and 45% of complaints against Instant Cash Loans Limited.

chapter 3

a closer look: analysing a sample of the complaints received in 2013/14

3 a closer look: analysing a sample of the complaints received in 2013/14

To dig deeper into the reasons underpinning consumers' complaints about payday lending, we analysed a sample of some of the complaints we handled in the 2013/14 financial year. This chapter gives more detail about the consumers, lenders and loans represented in the sample of complaints we reviewed.

snapshot

- The profile of the consumers represented in our sample of 353 complaints (age, gender, geographical region) closely matched the overall profile of those complaining to the ombudsman about payday loans in 2013/14.
- In almost one in eight cases (13%), consumers in our sample had brought their complaint to the ombudsman with help from a relative, friend or carer. We did not see evidence of significant activity by claims management companies (CMCs).
- Over a third of the consumers in our sample had brought a previous complaint to the ombudsman, and we also saw evidence that many had taken out previous payday loans.
- The sample included complaints against 46 different businesses, with WDFC UK Ltd (Wonga) accounting for the largest proportion of reviewed cases (31%).
- In the majority of complaints reviewed, consumers had initially borrowed £500 or less, although some had borrowed in excess of £1,000. In over half of the sampled cases, loans were still ongoing at the point of the consumer's complaint to the ombudsman.

methodology

Payday loans are short-term, unsecured credit products, generally taken out for 12 months or less, and where the amount borrowed is usually less than £1,000. In selecting our sample of payday loan complaints to focus on in more detail, we were guided by the CMA's working definition:

"*Small-sum cash loans marketed on a short-term basis, not secured against collateral, including (but not limited to) loans repayable on the customer's next payday or at the end of the month and specifically excluding home credit loan agreements, credit cards, credit unions and overdrafts.*"[17]

Our selected sample was also consistent with the FCA's definition of high-cost short-term credit (HCSTC).[18]

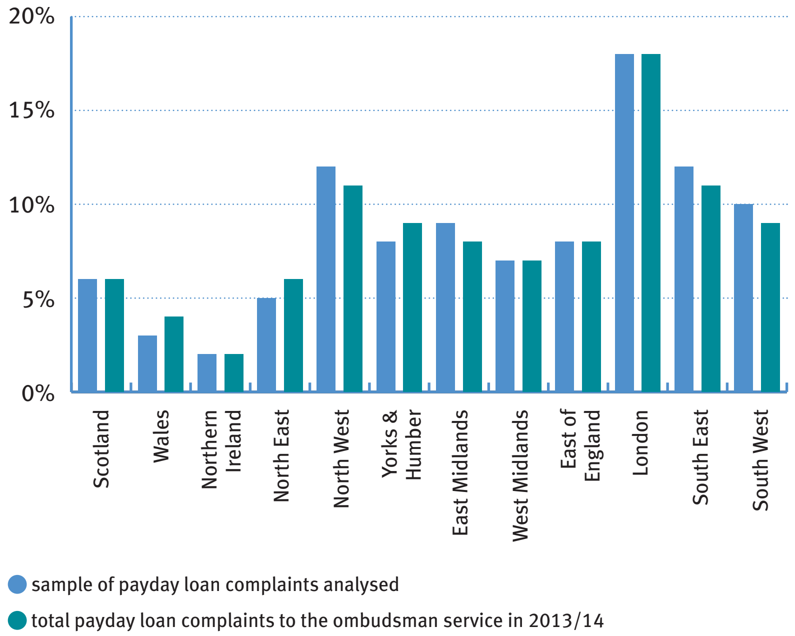
We did not look at other short-term high-cost credit products such as logbook loans (secured against a vehicle) and short, fixed-term instalment loans, nor did we include debt collection complaints that related to payday loans, as these complaints were levelled at the company collecting the debt rather than the lender(s) from which the consumer's loan(s) originated.

We looked at all payday complaints that had both opened and closed since the start of the last financial year (April 2013). This generated a sample of 353 individual cases between 1 April 2013 and the start of our review, which began on 21 February 2014. We used management information data collated from complaints cases to look at demographic information about the consumers.
We then reviewed the 353 individual files to glean more information about what had gone wrong and why the consumers had referred their complaints to the ombudsman service.

Areas of focus in our analysis included identifying the main and subsidiary reasons for consumers' complaints; the size of the loans complained about, and their date of issue; whether the loans had been topped up or rolled over; and whether or not the consumers' complaints had been upheld. We also reviewed the complaint files for evidence about the consumers' circumstances which may have had a bearing on their complaint, for example obvious evidence of financial hardship, unemployment, or serious illness. We also looked for evidence on how businesses had handled the complaints, particularly with respect to vulnerable consumers.

Following the completion of the file review, a series of follow-up interviews were conducted with adjudicators and ombudsmen working in the ombudsman service's consumer credit division. This was designed both to gather further qualitative insight into the payday loan complaints we receive, and to discuss the themes arising from the review.

figure 8: regional distribution of consumers in the sampled payday loan complaints



source: Financial Ombudsman Service.

the consumers represented in our sample

age, gender and region

The profile of the consumers represented in our sample of 353 payday loan complaints was consistent with the overall profile of those bringing complaints to the ombudsman service about payday loans in the 2013/14 financial year. 62% of the consumers in the sample were men (compared to 60% overall) and 38% women (40%). Consumers aged between 25 and 34 comprised the largest group within the sample and in the overall complaint figures (both 32%). And the regional distribution was almost identical, as figure 8 illustrates.[19]

"There are a number of reasons why consumers might use a representative. They may lack the confidence to deal with their problem, have issues such as an illness to contend with, or be in denial about their debt position. Often we see younger people whose parents complain on their behalf."

Mark Hollands, ombudsman

table 3: did the consumer bring the complaint themselves or were they represented?

consumers brought complaint themselves	**84%** (296)
consumer was represented by family/friend/carer	**13%** (46)
consumer was represented by a claims-management company	**1%** (3)
other representation	**2%** (8)

base: 353 complaints.

representation

As shown in table 3, in the vast majority of cases we reviewed (84%), consumers had brought their complaint to the ombudsman service themselves. However, in 13% of the sampled complaints, consumers were represented by a relative, friend or carer. Evidence of representation by claims-management companies (CMCs) was negligible, featuring in just 1% of the sample.[20]

In the follow-up interviews we undertook as part of our research, adjudicators and ombudsmen told us that a variety of reasons can explain why a consumer might be represented by another person rather than bring the complaint themselves. The personal circumstances of some consumers may be such that they don't feel able to cope with the stress of pursuing a complaint. Adjudicators said that when family members bring a complaint on someone's behalf it can be because they recently found out about the payday loans and are trying to help. This was particularly the case with representation by parents, who sometimes also repay the balance owed on behalf of their child.

previous complaints

Interestingly, just over a third (36%) of the consumers represented in the sample had previously complained to the ombudsman service, with 28% of these consumers having prior complaints relating to payday lending, as shown in table 4.

table 4: at the point of the complaint, had the consumer previously complained to the Financial Ombudsman Service?

yes	**36%** (116)
no	**64%** (207)

base: 323. The 353 complaints in the sample were brought by 323 individual consumers. 21 consumers had brought multiple complaints. For the purposes of this table, the individual consumers represented in the sample are counted just once – at the occasion of their first complaint about a payday loan to the ombudsman service.

The proportion of our sample with previous complaints to the ombudsman is higher than we might have expected. The ombudsman service already undertakes a significant amount of outreach work to boost awareness of what we do and how we can help, including around payday lending. But the fact that more than one-in-three of our sampled consumers had previously complained to us might suggest a lack of awareness about the ombudsman service among consumers in the payday lending market. Responding to this finding, the ombudsman has launched a campaign to increase awareness of the help we can provide and to urge consumers struggling with any form of debt to seek free and impartial help.[21]

previous payday loans

In our review we looked for evidence of whether consumers bringing complaints to us had previously taken out another payday loan. While in two-thirds of cases (65%) it was not possible to determine on the basis of the information available in the ombudsman case files, in a third (34%) it was clear that the loan at the heart of the complaint was not the consumer's first.[22] This is also consistent with what we heard first-hand from adjudicators and ombudsmen, who told us that consumers bringing complaints about payday lending frequently have multiple payday loans at any one time, or have taken out a number of sequential payday loans. Consumers in financial hardship were also much more likely to have had previous loans. Some of the consumers in our sample had had 10 or more previous payday loans from the same lender.

the businesses represented in our sample

Our sample of 353 complaints comprised complaints against 46 different businesses. The lenders represented are listed in table 5 below. The distribution broadly reflects that seen in our overall payday lending complaint figures, with WDFC UK Limited accounting for the largest number of cases in our sample (110), reflecting the size of their market share.

table 5: the businesses represented in our sample

lender	number of cases reviewed	proportion of total reviewed
WDFC UK Ltd/Wonga	110	**31%**
Casheuronet UK	26	**7%**
Express Finance	25	**7%**
Instant Cash Loans	21	**6%**
Microcredit	21	**6%**
CFO Lending	17	**5%**
Lending Stream	16	**5%**
MEM Consumer Finance	16	**5%**
Web Loan Processing	10	**3%**
Ariste Holding	9	**3%**
Think Finance (UK)	8	**2%**
PDL Finance	7	**2%**
Active Securities	6	**2%**
Wage Day Advance	5	**1%**
Cash on Go	4	**1%**
Uncle Buck	4	**1%**
other	48	**14%**

base: 353 complaints.

"It is noticeable that a large number of consumers who bring complaints have had more than one payday loan – it is very rare that we see complaints about a consumer's first loan."

Robert, adjudicator

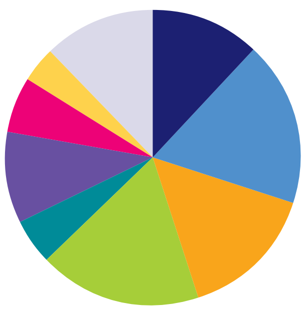
the loans at the centre of the sampled complaints

value of the loans in the sample

In 68% of the cases we reviewed, excluding those featuring an allegation of fraud, consumers had initially borrowed £500 or less (see figure 9) . This excludes any subsequent charges, fees or interest that may have been applied.

A greater proportion of our sample featured high value loans than was evident in the research conducted as part of the former Competition Commission's payday lending market investigation[23], as shown in figure 10 (overleaf). Excluding 'unknown' values from our sample of complaints, together with complaints incorporating allegations of fraud, 23% of cases featured initial loans of £500 or more. This compares to just 10% of loans studied by the Competition Commission. While we are not able to draw a causal link, it is clearly possible that the higher borrowing by the consumers represented in our sample was a contributory factor in their bringing complaints to the ombudsman.

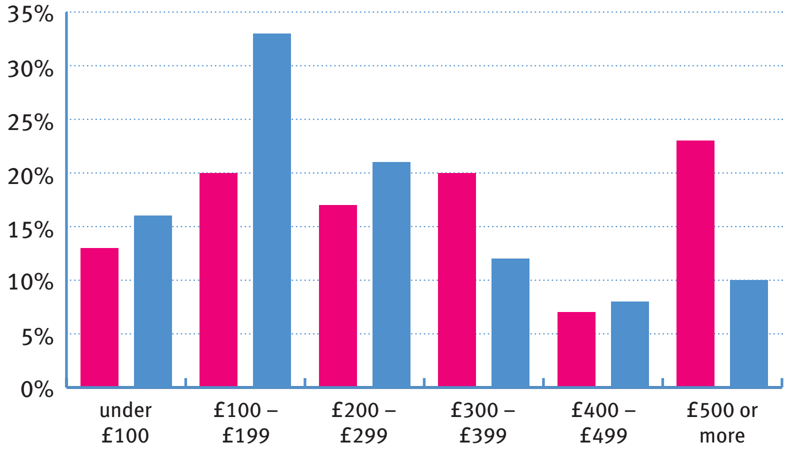
figure 9: amount of money consumers had initially borrowed



£1-100	12%
£101-200	18%
£201-300	15%
£301-400	18%
£401-500	5%
£501-750	10%
£751-1,000	6%
£1,000+	4%
Unknown	12%

base: 278 complaints, omitting cases incorporating suspicions or allegations of fraud.

figure 10: comparing the size of loans



source: Financial Ombudsman Service sample of complaints and Competition Commission, *Research into the payday lending market. Report*, January 2014, p. 37. To aid comparison between the two data sources, complaints incorporating allegations of fraud, and those where the size of the consumer's initial loan was unknown, have been omitted from the sample of ombudsman complaints.

when the loans were taken out

The date at which a consumer brought a complaint to the ombudsman service is not necessarily a good guide as to when the loan at the centre of the complaint was originally taken out. Of the cases reviewed, 1% concerned loans taken out in 2014, 28% loans taken out in 2013, and 29% loans from 2012. But just over a fifth of sample cases, 22%, concerned loans taken out in 2011 or earlier. In 68 cases (19% of the sample), it was not possible to tell from the case file when the loan was taken out.

> "While the intention is to borrow a small amount over a short term, often we see that this does not reflect reality – particularly for those experiencing financial hardship."
>
> **Amanpreet, adjudicator**

how long the payday loans had been running

Disregarding those cases featuring allegations of fraud, a noticeable feature of the sample of cases reviewed was the length of time consumers' loans had been running. In over half of the non-fraud cases analysed (57%), consumers' loans were ongoing at the point of complaint to the ombudsman service. In a further 17% of cases, loans had lasted in excess of 76 days. See table 6.

The high proportion of ongoing loans is likely to be due in part to the number of consumers in our sample who were experiencing financial hardship.[24] The distribution will also reflect the fact that by the time cases reach the ombudsman service, something has gone wrong which the business has not been able to resolve to the consumer's satisfaction. It is perhaps no surprise, then, that our snapshot of cases features very few instances of loans concluding in a short period of time. Indeed, in just 6% of the non-fraud cases we looked at had loans lasted for a month or less.[25]

table 6: length of loan that was the subject of the consumer's complaint

loan ongoing at time of complaint	**57%**	(158)
1-10 days	**1%**	(4)
11-20 days	**2%**	(5)
21-31 days	**3%**	(7)
32-40 days	**1%**	(4)
41-60 days	**4%**	(12)
61-75 days	**1%**	(4)
76 days +	**17%**	(48)
Unknown	**13%**	(36)

base: 278 complaints, omitting cases incorporating suspicions or allegations of fraud.

chapter 4

why consumers had brought complaints about payday loans

4 why consumers had brought complaints about payday loans

One of the central goals of the research was to develop our understanding of why consumers complain to the ombudsman service about payday loans and what that might tell us about common patterns in what is going wrong. This chapter sets out our findings on the reasons driving consumers' complaints to the ombudsman in the sample of cases analysed.

snapshot

- Payday lending complaints were often found to be multi-faceted rather than single-issue, featuring a combination of reasons for complaint.
- There was no single, dominant reason for consumers' dissatisfaction. Instead, the case files analysed featured a broad spectrum of issues.
- The review looked at the main feature of consumers' complaints and also subsidiary features of complaints, where possible to identify.
- The most frequently occurring main features of complaints were: allegations of fraud; poor administration; the unauthorised/unexpected taking of funds; and lenders ignoring debt repayment plans.
- Taking the main and subsidiary features of complaints together, the leading issues were found to be: damage to credit records; poor customer service; and poor administration.

figure 11: main reason for consumers' complaints about their payday loan

allegation of fraud	16%
poor administration	14%
unexpected taking of funds	13%
repayment plan not accepted	13%
damage to credit record	12%
aggressive debt chasing	6%
unaffordability	5%
high interest rates	4%
misleading information	3%
poor service	3%
high charges	3%
rollovers	1%
other credit application rejected	1%
other	4%
unknown	1%

base: 353 complaints, including cases incorporating suspicions or allegations of fraud.

main reason for complaints

For each complaint reviewed, the review team aimed to identify both the main reason for the consumer's complaint and also any subsidiary reasons that were apparent from the case file. The results present a surprisingly balanced picture. No single dominant reason for consumers' complaints emerged among the spread of main issues identified, as figure 11 illustrates.

> "There is no single stand-out reason for complaint in the payday loan cases we see. Many are linked to financial hardship and poor business practice."
>
> **Rupy, adjudicator**

Instead of one leading theme, five issues were particularly visible as main features of complaints, cumulatively accounting for 68% of the sample. These were:

- allegations of fraud
- poor administration
- the unauthorised or unexpected taking of funds
- lenders ignoring or not accepting a repayment plan
- damage to the consumer's credit record

Beneath these leading issues lay a further eight factors, including complaints focused on aggressive debt-chasing, irresponsible lending, high costs, poor customer service and the negative impact of payday loans on other credit applications.

Again, these reasons for complaint were relatively evenly distributed across the remainder of the sample, as table 7 shows.

all reasons for complaint

When we take *all* observable factors of a complaint into account, instead of focusing on the principal discernible reason, a subtly different picture emerges. Adding together all appearances of an issue across the sampled complaints, damage to credit records and poor customer service rise to the surface as the most commonly observed features of complaints. See table 8.

Comparing the results of the 'main' and 'all' features of complaint tables, consumers' reasons for complaining about a payday loan might be divided into three loose groups. It is clear that some issues that featured prominently as main reasons for complaint remained significant issues when all features of complaints were factored in. We might term these issues as being of ***stable and high prominence*** across our sample of cases. Examples include consumer unhappiness with poor administration and the unexpected or unauthorised taking of funds from their account.[26]

> "The lack of a central complaint issue is likely due to the fact that, if one thing went wrong with the loan, it's likely another five connected things happened before."
>
> **Robert, adjudicator**

table 7: what was the *main* feature of the consumer's complaint about the payday loan they had taken out?

allegation of fraud	**16%**	(57)
poor administration (*eg* loan paid into wrong account, not registering payment)	**14%**	(49)
unauthorised/unexpected taking of funds	**13%**	(47)
lender ignored/did not accept repayment plan	**13%**	(45)
damage to credit record	**12%**	(42)
lender aggressively chasing for debt	**6%**	(22)
unaffordability (at the point loan was taken out, *ie* irresponsible lending)	**5%**	(19)
high interest rates	**4%**	(15)
misleading information (including mis-sale)	**3%**	(11)
poor customer service (*eg* failure to return calls, rudeness)	**3%**	(11)
high charges	**3%**	(10)
rollovers	**1%**	(5)
application for other credit rejected (*eg* mortgage, overdraft)	**1%**	(3)
other	**4%**	(14)
unknown	**1%**	(3)

base: 353 complaints, including cases incorporating suspicions or allegations of fraud.

table 8: *all* features of consumers' complaints about the payday loan they had taken out

damage to credit record	**24%**	(85)
poor customer service (*eg* failure to return calls, rudeness)	**21%**	(73)
poor administration (*eg* loan paid into wrong account, not registering payment)	**20%**	(69)
unauthorised/unexpected taking of funds	**19%**	(68)
lender ignored/did not accept repayment plan	**18%**	(65)
lender aggressively chasing for debt	**18%**	(64)
allegation of fraud	**16%**	(58)
high charges	**16%**	(56)
high interest rates	**12%**	(44)
unaffordability (at the point loan was taken out, *ie* irresponsible lending)	**7%**	(26)
misleading information (including mis-sale)	**5%**	(18)
rollovers	**5%**	(17)
application for other credit rejected (*eg* mortgage, overdraft)	**3%**	(10)
other	**12%**	(43)

base: 353 complaints, including cases incorporating suspicions or allegations of fraud. Totals include all discernible features of complaints, including the main feature.

Stable high prominence	• poor administration • unauthorised/unexpected taking of funds • ignoring/not accepting debt repayment plan • [*fraud*]
Increasing prominence	• poor customer service • high charges • damage to credit record • lender aggressively chasing for debt • high interest rates
Low prominence	• rollovers • application for other credit rejected • misleading information • unaffordability

Some issues which were not especially prominent in the list of main reasons for complaint remained less significant issues when all components of complaints are taken together. We might consider these issues as being of relatively ***low prominence*** across the sample, with examples including rollovers and the rejection of other credit applications as a result of having taken out a payday loan.

Most interestingly, some issues become considerably more conspicuous when all discernible features of complaints are taken together, and clearly form the backdrop to a much higher proportion of complaints without necessarily being the initial trigger cause. We might term features in this category as being of ***increasing prominence*** the more closely we examine each case. The category includes some issues that might have been expected to feature more strikingly as principal drivers of consumers' complaints about payday loans, such as high interest rates and high charges.

multi-faceted complaints

The majority of complaints we reviewed in the sample were found to be multi-faceted: they tended to comprise a variety of interwoven factors. Two-thirds (64%) of the sampled cases featured more than one strand to the complaint, and in a quarter (26%) of cases there were three or more elements. Omitting complaints involving an allegation or suspicion of fraud, which tended to be single-issue cases, 71% of the sample featured multiple aspects to the complaint.

This picture of multi-dimensional complaints perhaps helps to explain the fact that we found no single issue dominating consumers' reasons for bringing a complaint to the ombudsman service. It is a picture that also emerged strongly in the complementary qualitative interviews undertaken among ombudsmen and adjudicators working in the service's specialist payday lending team.

Those handling payday lending cases remarked on the fact that, while it is difficult to define a 'typical' payday complaint – owing to consumers' varied reasons for borrowing and personal circumstances – many of the same issues nevertheless arose time and again. For instance, a consumer might be unhappy that their loan repayment was not processed by a lender on time, subsequently leading to a late payment marker. The backdrop to many such cases can be – in the consumer's eyes – poor business practice and customer service, an issue we return to in a later section.

> "Complaints are multifaceted as the issues are linked. Credit file issues arise from pretty much every case we see. If a loan was unaffordable, then the consumer won't appreciate the payments being taken through a CPA. Financial hardship is also often entwined."
>
> **Mark Hollands, ombudsman**

chapter 5

complaints about fraud

5 complaints about fraud

It is widely recognised that fraud presents a major challenge for the payday loan industry. The Office of Fair Trading, the former sector regulator, observed last year that "it is difficult to quantify how much fraud the sector is subject to, but the growing incidence of complaints is a matter of significant concern to us."[27] Complaints about a loan the consumer said they had not taken out featured strongly within the payday complaints we reviewed – it was the most frequently-occurring main reason for complaint in our sample. This chapter looks at the content of some of those complaints and how they were handled by the business.

snapshot

- Complaints from consumers that they had not taken out a disputed loan were highly prominent within the research sample, with one in six cases featuring an allegation of fraud.
- Different types of fraud were seen in complaints, from alleged identity theft and phone-based scams to fraud perpetrated by someone known to the consumer.
- Younger consumers in the sampled complaints were more likely to complain about fraud than older consumers.

The UK's Fraud Prevention Service, CIFAS, recorded a 55% annual increase in fraud on loan accounts in 2013, and pointed to the "rapid emergence of payday lending" as one of the main drivers:

"... *payday lenders have quickly become known as a speedy and convenient way to obtain money with relative ease. The very convenience that is an attractive selling point has, of course, proved extremely tempting to the fraudster* ..." [28]

While identity fraud occurs across the banking and consumer credit sector, it is suspected that the design of payday loans has made them a particular target for fraudsters, as highlighted by CIFAS. Ombudsmen interviewed in our research said that the speed of the application process and lack of checks can seemingly allow fraudsters to slip through the net.

The OFT also raised concerns last year about the ability of loans to be paid into a bank account held in a different name to that of the applicant.[29]

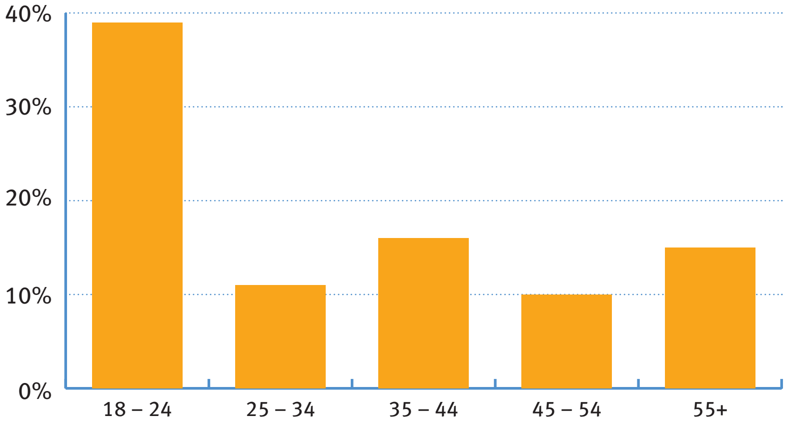
Where an allegation is made that a loan was not taken out by the consumer, the ombudsman service uses evidence to determine, on the balance of probabilities, whether or not the consumer took out the loan, and will look at a number of factors when considering these types of complaint.

In some of the complaints we reviewed, the lender had already accepted the loan was fraudulent but the consumer was complaining about a related issue. For example, the customer service and time taken in resolving the matter may have been unacceptable; there may have been related bank charges because the lender had taken funds out of the complainant's bank account; or late payment markers might have been put on the consumer's credit file. The uphold rate on fraud cases within the sample was 61%, in line with the overall uphold rate.

Looking more closely at the complaints in our sample, we found that younger consumers were more likely to complain that they hadn't taken out a disputed loan. As illustrated in figure 12, alleged fraud was the main reason for complaint of 39% of those in the 18 to 24 age group, compared to 15% among the over-55s.

> "Some consumers have a lack of awareness about the risks of sharing personal details, for example on social networking websites."
>
> **Amanpreet, adjudicator**

figure 12: fraud as the main reason for complaint, by age of consumer



source: Financial Ombudsman Service sample of payday loan complaints.

Adjudicators suggest that some younger people may be targeted because they have shared key personal information, such as their date of birth, on social network websites. But all age groups can be vulnerable: adjudicators pointed to examples of older people being susceptible to fraud because they were less aware of potential scams.

different types of fraud

A wide variety of different scenarios were seen within the complaints, including identity theft, scams, fraud allegedly perpetrated by somebody close to the consumer, and occasions where the alleged fraud could not be proven. Broadly speaking most businesses did take allegations of fraud seriously and would investigate a case. Below we review examples of the different types of fraud we saw in the sample.

Identity fraud, where a fraudster had applied for a loan in the name of someone else, was common in the cases we reviewed. This seems to be a problem in the market: a Citizens Advice survey of a sample of payday loan cases it dealt with in the first six months of 2013 found that one in five involved a consumer being chased for a loan they had not taken out.[30]

Our sample included cases where fraudsters had seemingly obtained personal information about the consumer (typically their name, address and date of birth) and stolen bank details in order to apply for a loan. Funds could then be paid into a different account, unrelated to the victim of the identity theft.

> "Fraud is a big problem in the complaints we see against payday lenders. Payday loans are marketed as quick and easy but this means detailed checks can be sacrificed."
>
> **Mark Hollands, ombudsman**

Often, the first the affected consumer knew of the crime was when money was debited from their bank account for the loan repayment. The case study below gives an example from our research. The case also highlights how closely linked fraud complaints can be with those about damage to credit files (a theme we address in more detail in the following chapter). Almost one in five of the cases in our sample where the main complaint was that the loan hadn't been taken out by the consumer also featured a related complaint about damage to a credit file.

case study

consumer learned of fraud after £200 was debited from their account

Four loans were applied for in Miss D's name. The first Miss D knew of the fraud was when the lender debited more than £200 from her account. It then emerged that the lender had tried to take further funds but the debits were unsuccessful. The loans were marked as 'in default' and were recorded on Miss D's credit record. After the consumer complained, the lender investigated and accepted the loans had been taken out fraudulently. The business removed Miss D's name from the loans and amended her credit file. But Miss D felt she should have compensation for the distress and inconvenience caused in getting the matter sorted out. The ombudsman service adjudicator agreed, upheld the complaint and awarded compensation.

Loan scams, run by organised criminal fraudsters, also featured in our complaints sample. In some of the cases we reviewed, consumers had received calls purporting to be from well-known payday lenders offering to advance a loan. Agreeing, consumers had been asked to pay high flat-rate arrangement fees, but the promised loans never materialised. In other complaints, consumers suspected that the loan had been taken out by someone close to them, such as a relative, friend or former partner, without them knowing. One business referred to instances such as these as 'friendly fraud'. The following case study gives an example.

case study

ex-partner took out numerous loans in victim's name

The payday lender was holding Mr C liable for loans he said he had not applied for and knew nothing about. Mr C said the loans had been paid into a joint account without his permission and subsequently withdrawn. Debits from his account had failed and defaults were placed on his credit file. The adjudicator upheld the case. The evidence suggested Mr C had been defrauded by an ex-partner. The lender removed Mr C's name from the account, refunded all payments made and removed defaults from his credit file.

> "On the whole most businesses take fraud complaints seriously and investigate. They tend to acknowledge consumers' concerns."
>
> **Amanpreet, adjudicator**

Sometimes a consumer said that they had not taken out the loan in question, but this could not be proven. The case study below gives an illustrative example from the sample of cases we reviewed.

case study

payday loan complaint rejected as fraud could not be adequately proven

Mr A had previous payday loans but complained to the lender that one loan had been taken out fraudulently in his name and put in to his account. The lender investigated and reported that all the loans were applied for from the same computer, and that the address and mobile phone number used also matched that of Mr A. The ombudsman service adjudicator assessed that on the balance of probabilities, and giving appropriate weight to the documentary evidence available, it was fair to say Mr A had not given his personal details to anyone else, and that it was unlikely anyone else had access to the computer. The complaint was not upheld.

chapter 6

complaints about damage to credit records

6 complaints about damage to credit records

Many of the consumers in our sample of complaints were concerned about the long-reaching impact of information recorded about their payday loan on their credit file. But it emerged there was also a widespread lack of understanding about how personal credit files work in practice. This chapter reviews what we found.

snapshot

- Complaints about damage to credit files featured in one in four cases (24%). This was the single most common issue of concern across the sample when all aspects of the complaint were considered.
- 12% of cases cited damage to a credit file as the main reason for complaint – the fourth most frequent 'main' reason.
- There was widespread misunderstanding about how credit reference agencies and personal credit files work, with many consumers asking for correct default notices to be 'wiped' from their file.
- 18% of cases where the main complaint was an allegation of fraud also featured a complaint about damage to a credit file.
- Some consumers complained they had been misled by the lender that a payday loan would improve their credit score.

complaints about credit file damage

Damage to a credit file was the fourth most frequent 'main' reason for complaint in the payday loan cases we reviewed, and overall featured in a quarter of all the sampled complaints – the single most common issue of concern. See table 9.

table 9: reasons why consumers had complained to the ombudsman service about payday loans

	main feature of complaint	all features of complaint
Damage to credit record	**12%** (42)	**24%** (85)

base: 353 complaints, including cases incorporating suspicions or allegations of fraud.

Complaints about damage to a credit file were frequently interwoven with other issues in the cases we reviewed. This is not surprising given the high proportion of consumers in our sample who were in financial hardship: many of these consumers will have had repayment problems and defaults recorded against them. While consumers were prompted to complain about damage to their credit file for a number of different reasons, one of the most frequently repeated themes was anger over the issue and recording of default notices.

recording defaults

A lender will usually issue a default notice in writing once a borrower has missed a number of repayments – this is typically when the consumer is between three and six months in arrears.

The default is recorded on the consumer's personal credit file. This information is held by three credit reference agencies (CRAs) – Callcredit, Equifax and Experian. Lenders are only required to issue a default notice for debts regulated by the Consumer Credit Act.

Lenders are obliged to report all payment information to the CRAs, including repayments made on time, late payments, missed payments and defaults. Consumers can obtain their statutory credit file for £2 from the CRAs.

In the case of a default the lender will report the default amount and date to the CRA.

> "Many consumers – not just payday loan borrowers – don't have a clear understanding of how credit records work. More needs to be done to better inform people, particularly vulnerable groups and those who have had problems with credit."
>
> **Mark Hollands, ombudsman**

A default will stay on the consumer's credit file for six years. This can seriously impair their ability to get credit. The majority of consumers in our sample were highly sensitive to this and understood the long-reaching implications of a default. One ombudsman noted that, "Even among those consumers with little financial understanding there is a fear of the wider reaching impact of credit file information. For those in financial difficulty it can be a particular area of concern."

Prominent among those concerns is the ability to obtain future credit. This can be an acute problem as payday borrowers may struggle to find affordable credit. Research commissioned by the Competition and Markets Authority found that as many as 39% of payday loan customers have no access to other types of credit, such as overdrafts or credit cards,[31] that three in ten have been turned down for credit in the past 12 months and that 52% have experienced debt problems in the past five years.[32]

Many of the complaints we saw were about a default being issued too soon – without sufficient notice. In some cases a default notice had not been sent out before the default was registered with the CRA. According to guidance produced by the credit industry in collaboration with the Information Commissioner's Office, lenders should notify consumers of their intention to register a default against them at least 28 days before doing so, to give consumers time to make an acceptable payment or reach an agreement with the lender on an arrangement.[33]

Other consumers felt the default should not have been issued at all. In the following example, typical of many we saw, the lender had failed to issue the correct notice of default.

case study

business fails to follow guidance by not issuing default notice

Due to financial problems Mrs S fell behind with her loan repayments. The lender sold the debt on to a debt collections agency who told her a default had been registered against her name. She complained to the lender stating that she had not been informed before the default was issued. She asked the business to send a copy of the default notice but despite repeated requests it did not respond. Only following intervention by the ombudsman service did the lender accept an error had been made and that it had not in fact issued a default notice to the consumer. The complaint was upheld and the lender was required to remove the default recorded with the credit reference agencies.

understanding credit files

Our review of cases revealed that many consumers showed a lack of understanding about how and why CRA information is recorded.

Research conducted by *Which?* in May 2014 supports the view that credit files are a difficult area for consumers to navigate. Its survey found that consumers felt CRA information to be jargon-filled and confusing. Fewer than half of those participating in the Which? research said that seeing their statutory credit report had given them a better understanding of their credit-worthiness.[34]

> "Many consumers don't understand their credit file. Even where a business is doing the right thing, the consumer often feels the information should not be recorded."
>
> **Rupy, adjudicator**

In the complaints we reviewed, it was common for the borrower to ask the payday lender to 'wipe' or otherwise remove information from their credit record. In practice, businesses are obliged to record accurate information with the CRAs, including where payments are not made, are made late or are insufficient. Accurate information of this kind cannot be removed as this is the data businesses use when assessing a potential borrower for credit. It is also an important protection against fraud.

A number of lenders, including Wonga, Quick Quid, Uncle Buck and Pounds to Pocket, have signed up to a real-time credit information service through Callcredit. The information, which is updated daily, aims to give the most up-to-date picture of a borrower's credit history. Previously data was shared monthly, which doesn't fit particularly well with the short-term nature of payday loans.

The following case study demonstrates how consumers can be confused about data held at the CRAs and the terminology used.

case study

consumer requests default be removed from credit file

After purchasing his personal credit file because of debt problems, Mr L became aware there was a default recorded for a previous loan. Mr L complained that this should be 'wiped' because he felt this loan debt had been settled – with a reduced figure agreed. He also argued the lender had not given him sufficient notice of the default. The credit file said the debt was 'partially settled' and the consumer felt it should say 'fully settled' as the loan was paid off. The adjudicator did not uphold the complaint, considering that a default notice had been sent within the correct time frame and that the consumer had been informed that the default would stand even after the partial settlement. The adjudicator also explained that the partial settlement was correct because the lender had agreed to 'write off' part of the debt and settle with a reduced figure.

case study

consumer is unhappy that fraudulent loans caused damage to credit file

Mr P was a victim of identity fraud and a number of loans were taken out with the same lender in his name. Mr P was not aware of the crime until demands were made for payment. The issue was resolved with the lender accepting fraud had taken place, but the 'missed payments' had resulted in marks on the consumer's credit file. Mr P asked the lender to instruct the CRAs to remove the incorrect data against his name, but this was not resolved for many months. The lender agreed to pay the costs Mr P had incurred in buying his credit file each month to check if the data had been removed. It also paid compensation for the trouble and upset caused. But Mr P did not feel this was enough, and escalated the complaint to the ombudsman. The adjudicator did not uphold the complaint, considering that the lender's offer was reasonable.

fraud and damage to credit files

Many complaints about fraudulent payday loans also featured a related complaint about the damage it had done to the consumer's credit record. In 18% of cases where the main reason for the complaint was an allegation of fraud, there was a subsidiary complaint about credit file damage. The case study example to the left is typical and shows how fraud and damage to credit files can go hand-in-hand. Although the consumer's request for an increased compensation offer was rejected by the adjudicator, the background to the case reveals how the credit file issue was pressing for the consumer.

misleading information

There has been increasing media coverage about how other lenders view the presence of payday loans on consumers' credit records, and how this might affect the credit applications of those consumers who had previously taken out a payday loan.[35]

Some of the cases we reviewed featured complaints by consumers who felt they had been misled by lenders as to the likely impact of payday loans on their credit records. A small number of consumers said that they had deliberately taken out payday loans to improve their credit rating, citing lenders' claims that repaying on time would be beneficial, but had subsequently experienced being turned down for other lines of credit, such as credit cards and overdrafts. Some consumers reported problems remortgaging.

In these complaints, while small in number, consumers argued that the very fact of having a payday loan had damaged their credit score and creditworthiness in the eyes of other lenders, even though the loan had been repaid on time. Consumers felt that other lenders, such as high street banks, credit card and personal loan providers, viewed payday loans negatively – or saw their borrowers as high risk, even where there are no recorded late payments or defaults.[36]

Potential lenders review a consumer's credit history by looking at their credit file. They then build an individual credit score for the consumer based on their repayment history and borrowing patterns, as well as other factors, which might include the consumer's employment status. These scores are individual to each lender and are usually commercially sensitive.

The provision of misleading information and the rejection of other credit applications were not common features in the sample of cases we reviewed, together accounting for 4% of the main reasons for complaint. Adjudicators and ombudsmen also reported that it is difficult to uphold complaints of this kind. This is because the consumer would need to show that the payday loan application itself had been responsible for the rejection for another line of credit, rather than any other factor or combination of factors. As one ombudsman commented: "Often a borrower has had other credit problems in the past so it is not possible to point to the payday loan and say this exclusively was the reason for the declined credit."

> "We would need to see that the wrong advice was given and the consumer would need to prove the payday loan affected their ability to get credit – that is, it caused them to suffer financially. It is often difficult to prove that it was the payday product alone that caused the rejection for other credit."
>
> **Juliana Francis, senior ombudsman**

chapter 7

complaints about debt-chasing, poor administration and customer service

7 complaints about debt-chasing, poor administration and customer service

Our review uncovered a range of inter-related complaints from consumers unhappy with the manner in which they had been chased for debt, the way lenders had administered loans, and the quality of lenders' customer service. In this section we look in more detail at the key themes arising.

snapshot

- The experience of those struggling to repay loans is of particular policy and regulatory interest, and our sample included numerous examples of consumers having problems agreeing a suitable repayment plan with their lender.
- We also saw many instances of consumers complaining about what they felt to be aggressive debt-chasing by lenders. This could be particularly stressful for those with mental health illnesses.
- Behind allegations of fraud, poor administration by lenders was the second most frequently observed main feature of the complaints we reviewed.
- Complaints about poor administration covered a diverse variety of issues, including loans paid into the wrong account, the miscalculation or misapplication of fees and charges, and repayments not being received or registered.
- While featuring less prominently as a main reason for complaint, poor customer service was a thread running through many of the cases we looked at, often exacerbating the effect of other issues.

what we found

Our review of complaints unearthed some issues you might expect when looking at a selection of payday lending cases, such as consumer concern about high interest rates and charges. But we also uncovered a high degree of consumer unhappiness about more 'everyday' business practices of payday lenders, with a failure to quickly correct a mistake often compounding the effect of the original error. In the following sections we look at the numerous different ways in which this found expression, from sloppy administration (such as lenders paying loans into the wrong account) to poor customer service.

We also look at a further significant theme of complaints: consumers who were unable to agree a debt repayment plan with their lender, or who were unhappy at how they were being chased to repay outstanding amounts.

debt repayment and collection

In advance of assuming responsibility for the regulation of consumer credit, the FCA announced that one of its first actions would be to review how payday lenders collected debt and managed forbearance and consumers in arrears.[37]

table 10: reasons why consumers had complained to the ombudsman service about payday loans

	main feature of complaint	all features of complaint
lender ignored/did not accept repayment plan	**13%** (45)	**18%** (65)
lender aggressively chasing for debt	**6%** (22)	**18%** (64)

base: 353 complaints, including cases incorporating suspicions or allegations of fraud.

Explaining the priority attached to investigating these issues, the FCA noted that one in three payday loans were repaid late or not at all, equating to over 3 million loans a year.[38]

Consumers who were struggling to repay the payday loans they had taken out were a particular focus of our own review. Within the sampled complaints we saw considerable evidence of consumers encountering problems agreeing a debt repayment plan with a lender, or expressing unhappiness with what they felt to be insensitive debt collection practices (table 10). These issues were often interlinked.

The treatment of those having problems repaying is obviously particularly important given the financial insecurity of many in this position. Of the 45 cases in our sample where the main feature of the complaint was the lender not accepting or honouring a repayment plan, all but one involved a vulnerable consumer, that is to say a consumer who – on the evidence available in the case file – was experiencing obvious financial, medical or personal difficulties.

As described elsewhere in this report (see chapter 9), and is well understood, payday loan debts can quickly spiral for those struggling to repay due to the effect of cumulative interest charges and fees for late payments. Our sample contained numerous instances of consumers having difficulty meeting a contractual repayment but being unable to agree a suitable alternative repayment plan with their lender.

The disagreement could be over the application of further charges and fees, the amount it would be reasonable for a consumer in difficulty to repay, or an appropriate schedule for the repayment. In a number of the complaints we reviewed the lender and consumer agreed a repayment plan following the involvement in the case of the ombudsman service. While this facilitation can be a key part of our role, it would clearly be better for agreement about an appropriate repayment plan to be reached before it becomes necessary for a consumer to refer the issue to the ombudsman.

We also saw many instances of consumers complaining about the aggressive pursuit of debt by lenders. These complaints had some common threads, particularly where lenders had not accepted (or processed) a debt as having been repaid. In these cases consumers were unhappy to receive letters or calls from debt collection companies relating to loans they believed they had paid off. Some consumers found some of this contact threatening and felt harassed. The combination of chasing letters and calls, added charges, the taking of further payments, and the passing of debts to third parties, were at the heart of a number of the cases we reviewed. Some were further aggravated by consumer perceptions of poor administration or poor customer service.

case study

lender fails to engage with a consumer trying to set up a repayment plan

Having taken out a loan, Mr G subsequently ran into financial difficulties. He contacted the lender to say he would be unable to make the scheduled payment. He requested a repayment plan and asked that the lender freeze interest and charges. Mr G made repeated attempts to contact the lender but it did not respond. The lender eventually replied approximately a month later, suggesting a repayment plan that the customer did not feel was reasonable. Reviewing the case, the ombudsman service did not consider that the lender had responded positively or sympathetically to Mr G's financial difficulties. In settlement of the complaint, the lender agreed to reduce the outstanding balance, set up a fair repayment plan and to make a payment to the consumer in recognition of the trouble and upset caused by its handling of the complaint.

Some of the consumers in our sample had linked complaints against debt collection companies. Although it is not possible to quantify the extent of this possible connection in our overall caseload on the basis of the sample of payday loan cases we reviewed, it was nevertheless a noticeable feature.

case study

a consumer is chased by debt collector to repay loan he had not taken out

Mr S received a letter from a lender advising him of an outstanding debt. Knowing nothing about the loan, he assumed it had been fraudulently taken out in his name. Unhappy at being threatened with court action for a loan he had not taken out, Mr S passed the crime reference number he had been given by the police to the debt collecting company acting on the lender's behalf. Following the consumer's complaint, the lender accepted that a mistake had been made and agreed to write off the debt. Some weeks later however, Mr S received a further letter saying that the balance was still outstanding and that the account had been passed to another debt collector. The letter had been sent in error due to the lender's system not having been updated.

" Administration can be poor, for example with payments not being recorded and websites giving inconsistent information. With business levels increasing, administration and complaints are often not dealt with proactively by businesses."

Stephen Cooper, ombudsman

Debt-chasing can be particularly stressful for consumers with acute mental health illnesses, and we saw some instances of consumers receiving chasing messages by text or email while hospitalised. In one case a lender explained that the root cause of the poor timing of some messages encouraging a consumer to repay was that the messages were automated, and therefore unable to discriminate between consumers in different circumstances. This was not accepted as a fair or reasonable explanation by the ombudsman, which felt that more care and attention should be taken when dealing with consumers in vulnerable circumstances.

poor administration

Behind allegations of fraud, poor administration by lenders – for example loans paid into the wrong account or payments not being registered – was the second most frequently occurring main reason for complaint we saw in the sample of cases reviewed. As shown in table 11, poor administration also featured strongly when all aspects of complaints were taken into account: a fifth of all cases in the sample included an element of poor administration.

As with our sample generally, complaints about poor administration were frequently intertwined with other issues, such as poor customer service and aggressive debt chasing – both of which we look at in subsequent sections.

case study

lender chases consumer insensitively for debt

Following a successful application for a loan which she subsequently had to roll over, Miss V was admitted to medical care for a mental health condition. A representative contacted the lender on the consumer's behalf to explain the situation, and asked that Miss V's account be put on hold to avoid interest and charges being applied. The lender said that it would require evidence of the consumer's situation, and that it would be happy to review the account once the evidence had been received. In the meantime, however, the business sent collections messages directly to Miss V's mobile phone to remind her that the loan was due. The representative argued that this had caused Miss V considerable distress at a difficult time. The ombudsman service upheld the complaint.

table 11: reasons why consumers had complained to the ombudsman service about payday loans

	main feature of complaint	all features of complaint
poor administration (*eg* loan paid into wrong account, not registering payment)	**14%** (49)	**20%** (69)

base: 353 complaints, including cases incorporating suspicions or allegations of fraud.

The case studies on this page illustrate the sorts of administrative errors consumers complained about. But there was a very diverse range, from miscalculated interest to the failure to respond to letters; from the failure to cancel loan applications within the relevant time period to the registering of defaults with credit reference agencies without notifying the consumer.

case study

consumer applies for a loan that is never paid, but is still chased for repayment

Mrs B applied for a loan but the funds were never paid into her bank account. She informed the business of this, and was told it would be investigated. The lender then started to chase her for repayment, saying she had not made the necessary payments, and added interest and charges. The lender then put a default notice on Mrs B's credit file and instructed debt collectors. The ombudsman upheld the complaint and made an award in recognition of the trouble and upset caused to Mrs B.

case study

discount incentive to take out a loan was not applied

Mr M was offered a cashback deal on his loan as an incentive. But having taken advantage of the offer, the discount was not applied. He repeatedly tried to get in touch with the lender by email, but received no reply. When he did eventually speak to the lender by telephone, he arranged a call back. This also never happened. Mr M was unhappy at the errors that had been made, the service he had received, and the charges incurred by calling a chargeable business rate telephone number to try to resolve the issue. The lender recognised the error, but part of the refund was not paid. The consumer's complaint was upheld by the ombudsman service. The lender was then late paying the required redress to the consumer, although eventually the money was paid.

case study

lender fails to process loan cancellation request, adding fees and charges

Having applied for a payday loan, a consumer with a mental health condition then asked for the loan to be cancelled within the 14-day 'cooling off' period. The lender failed to process the cancellation in time and the loan was issued. But the lender did not immediately take back the loaned sum and, when it did later attempt to recover the money, there were insufficient funds in Mr J's account. Fees and charges were added, and the debt passed to a recovery firm. When Mr J subsequently asked for the amount he needed to repay, he was quoted different amounts on different occasions by the lender. The debt-chasing had a significant negative impact on Mr J's condition. The complaint was upheld by the ombudsman service. The lender was ordered to write off the debt, remove all traces of the loan from Mr J's credit file and pay £200 in compensation for the trouble and upset caused.

poor customer service

While not featuring prominently as a principal cause for consumer complaints in our sample of cases, poor customer service was a strong background noise, as shown in table 12. As with poor administration, bad service often served to compound consumers' unhappiness about a different aspect of their original complaint, accelerating frustration and delaying the resolution of their problem. As one of our ombudsmen commented, poor customer service is a thread running through many of the payday lending complaints we see, and businesses' responses to consumers' complaints can – in the worst practice we see – simply morph into further demands for payment.

The case study opposite gives just one example of a consumer not receiving the service or treatment they expected when dealing with a lender. But poor service is inevitably difficult to disentangle from other elements of a complaint, and is implicit in many of the case studies we include elsewhere in the report. Consumers frequently expressed unhappiness at the way in which lenders had communicated with them as customers. This sometimes took the form of contact perceived to be disproportionate, for example in lenders' pursuit of outstanding debt. On other occasions consumers complained about inappropriate contact, such as when lenders telephoned them at work when consumers had specifically requested otherwise, or lenders being rude on the phone.

And consumers also complained about lenders being elusive when consumers *did* want to get in touch to raise an issue, for example by failing to return calls or emails within promised timescales, or by generally being inaccessible or unwilling to engage about a complaint, as our case study illustrates.

table 12: reasons why consumers had complained to the ombudsman service about payday loans

	main feature of complaint	all features of complaint
poor customer service (*eg* failure to return calls, rudeness)	**3%** (11)	**21%** (73)

base: 353 complaints, including cases incorporating suspicions or allegations of fraud.

> "We see many payday loan businesses that are focused on low overheads and high turnover. It means customer service can be neglected – it just doesn't appear to be a priority for many firms we see in this sector."
>
> **Juliana Francis, senior ombudsman**

case study

consumer told that the lender was unable to handle complaints itself

Mr F complained to the ombudsman service on behalf of a relative, who was no longer able to cope with the level of debt they had accumulated. Mr F had tried to communicate with the relevant lender to inform them of his relative's situation and to manage it, but found the lender difficult to deal with. Mr F claimed he was told by the lender that it was unable to deal with customer complaints itself, that there was no customer service or complaints team he could speak or write to, and that he should instead contact the ombudsman. Mr F found this odd and confusing, understanding that the ombudsman service should be a last resort. He argued that "This company needs to address their problems with customer service to those in difficulty." The complaint was upheld.

chapter 8

complaints about continuous payment authorities

8 complaints about continuous payment authorities

The FCA, which assumed responsibility for the regulation of payday lending in April this year, has scrutinised the way in which lenders collect repayments from borrowers via continuous payment authorities (CPAs). It found that some firms were using CPAs as a debt collection method, and has introduced tough new rules controlling their use. Complaints alleging that a CPA was used excessively or without warning were a common theme in our review, as this chapter details.

snapshot

- The unexpected or unauthorised taking of funds (via a CPA) from an account by a payday lender was the third most common (main) reason for consumers in our sample to bring a payday loan complaint to the ombudsman.
- Complaints about CPAs were repeated throughout the cases analysed even where they were not the main reason to complain. CPA misuse was cited as an issue, in total, in almost one in five complaints.
- Repeated use of a CPA after a consumer had defaulted or was in hardship was a frequent cause of complaint.

what were the complaints about?

CPA payments are set up using a debit or credit card. The CPA gives the lender the authority to take regular automated payments from the consumer, without needing permission each time, with the money being collected from the card – typically a debit card linked to a bank account. The day on which the payment is taken can vary, as can the amount.

A large number of consumers who brought payday loan complaints to the ombudsman service were unhappy about how CPAs had been used. As table 13 shows, more than one in ten complaint cases (13%) cited the unauthorised or unexpected taking of funds as the main reason for the complaint. And when subsidiary reasons to the complaint were recorded, this rose to 19% – almost one in five.[39]

The following case study demonstrates how the CPA can cause tension between consumer and lender.

table 13: reasons why consumers had complained to the ombudsman service about payday loans

	main feature of complaint	all features of complaint
unauthorised/unexpected taking of funds	**13%** (47)	**19%** (68)

base: 353 complaints, including cases incorporating suspicions or allegations of fraud.

case study

lender refused to stop CPA despite consumer's financial hardship

Following personal problems Mr W was forced to reduce his working hours which led to difficulties meeting loan repayments. He offered a reduced repayment plan to the lender and withdrew consent to the CPA. The lender claimed not to have received this notification and continued to debit funds from his account via the CPA on numerous occasions, exacerbating his debt problems. The ombudsman service adjudicator upheld the complaint. The business was told to reduce the outstanding balance owed by removing the interest and charges incurred after the consumer informed it of his difficulties.

In 2012, the four main trade associations representing payday lenders came together to produce a voluntary code of conduct for their member firms – the *Good Practice Customer Charter* for payday and short-term loans.[40] The Charter outlines how the industry aims to treat borrowers when using CPAs. It states that firms will:

"*Always notify you by email, text, letter or phone at least three days before attempting to recover payment using continuous payment authority on the due date. This notice will ask you to contact us if you are in financial difficulty and cannot repay.*"

But many of the complaints we reviewed related to the frequent use of a CPA after the loan due date, typically when the full amount of the repayment could not be recouped through the CPA or the consumer had defaulted on the loan.

One adjudicator said: "Firms usually send a reminder a few days before the repayment due date, but they don't tend to give any further notification after this, for example for further CPA attempts – of which there can be many." Indeed, we saw examples of businesses attempting to take payments using a CPA on consecutive days for an extended period of time.

This continual dipping into the consumer's account could often cause the borrower to incur bank charges, for example on an unauthorised overdraft. It could also leave the consumer without sufficient funds to pay for necessities such as rent and food.

New FCA rules limit the number of times lenders can unsuccessfully use a CPA to two. The regulator has also banned the use of a CPA for part payments – a CPA can only be used if it pays off the loan in full. Borrowers can re-set the CPA if they choose to roll-over or refinance the loan. Firms are now required to keep records to show the consumer has consented to further use of a CPA. It will also not be considered appropriate to use a CPA where a consumer is in financial difficulty.[41] Should we see systemic breaches of these new rules, we will alert the FCA.

The regulator has made it clear that businesses have an obligation to cancel a CPA at the request of the customer. The FCA has also stated that should a payment go through by mistake following a cancellation by a customer, then the customer would be refunded immediately.[42]

Unlike direct debits, there are no 'money back' safeguards for consumers with a CPA. For example, under the 'direct debit guarantee' customers can get a full and immediate refund from their bank for any payment taken in error. If payment dates or the amount change with a direct debit, the consumer will typically be notitified 10 days in advance of the payment.[43]

In its compliance review of the payday market, the Office of Fair Trading said CPAs had been the subject of a 'substantial number' of consumer complaints, such as the consumer not being aware that they had signed up to a CPA or how it would work, and lenders taking frequent part-payments over several days or weeks often leaving the consumer facing financial difficulties.[44]

Analysis of 665 payday loan customers who contacted Citizens Advice for debt help between January and June 2013 showed that 32% had complaints about a CPA, with one in six saying that the lender used a CPA to take more than originally agreed.[45] Separately, the FCA has also found evidence of payday lenders failing to communicate important information about the function of CPAs and how they differ from direct debits.[46]

The complaints seen at the ombudsman included cases where a CPA had been applied earlier than the borrower expected, so it came as a shock. In some cases, the use of the CPA in this way had led to bank overdraft charges or financial hardship. In other cases, consumers felt that too much money had been taken via the CPA or that the CPA had been used too frequently.

In our review of complaints we saw some examples of a friend or family member using their debit card to make a one-off payment to help the borrower pay off some of their debt, only for the lender to then start using a CPA on the card, as the next case study illustrates.

case study

father used debit card to pay off daughter's debt and was hit with CPA

After his daughter got into difficulties repaying her payday loan Mr P stepped in and offered to make a part payment towards reducing her outstanding balance. The payment was made over the phone using his debit card. At the time he made it clear this was to be a one-off payment and no permission was given for use of a CPA. However, in the following weeks the lender took various sums of money by using a CPA linked to Mr P's bank card, causing him to go into an unauthorised overdraft and incur high penalty fees from his bank. Mr P complained to the payday lender and was refunded the money taken through the unauthorised CPA but it did not compensate him for the bank charges. For this reason the complaint was brought to the ombudsman. The adjudicator upheld the complaint and told the lender to pay £150 in compensation and to cover the bank charges.

In some of the complaints we reviewed, the adjudicator considered that the lender had not used the CPA unreasonably despite the consumer's complaint. In these cases we were satisfied that the consumer was aware of and accepted that the lender was permitted to take payments from the registered card. That said, we would expect the lender to act reasonably and sympathetically, continue to try to contact the consumer and, where appropriate, freeze interest and charges.

> "Often the consumer is in difficulties and struggling to pay, only for the lender to repeatedly dip into their account. The unexpected and relentless nature of CPA can make the consumer's situation much worse."
>
> **Mark Hollands, ombudsman**

The next case study gives an example from our review sample of a lender showing good practice in demonstrating forbearance and proactively trying to communicate with the consumer.

case study

use of CPA not unfair as borrower was evasive

Mr K made a complaint about a number of payments he claimed the lender took without his permission. When Mr K missed the repayment on a one-month loan the lender tried to get in contact by phone, email and post but Mr K did not respond. The phone number he had given was incorrect. The consumer claimed he was unable to get in contact with the lender but the adjudicator considered that the lender had done the right thing and that the terms of the loan and the CPA agreement were made 'sufficiently clear' at the outset. The case was not upheld. Even so, the lender showed forbearance and wrote off a large part of the consumer's outstanding debt.

chapter 9

complaints about high costs and charges

9 complaints about high costs and charges

The high cost of payday loans has been one of the biggest criticisms of the industry by politicians, consumer groups and debt charities. This chapter looks at the complaints the ombudsman received about interest rates and charges, why the complaints were brought, and who brought them.

snapshot

- Although the cost of credit did not feature prominently as a primary reason for complaint, either one of high interest rates or high charges was cited as a contributory factor in many cases.
- Consumers who were in financial hardship were more likely to complain about high interest rates and charges.
- Complaints about charges tended to be about default and other penalty fees rather than up-front administrative, rollover or loan advance charges.

the high cost of borrowing

At the start of the research we anticipated to find that one of the main reasons consumers had complained about a payday loan would be its high cost.

Our findings in this respect were surprising. As shown in table 14, high interest rates were cited as the main reason for complaint in just 4% of the sampled cases we analysed. High charges were the main reason for complaint in 3% of the sample.

But this is only part of the picture. When complaints were further analysed to look beyond the main reason for complaint and take into account additional issues, in total 12% of cases mentioned high interest rates and 16% mentioned charges.

Interestingly, few consumers complained about upfront costs, such as the fees associated with setting up a loan or the headline interest rate (annual percentage rate – known as APR).

Ombudsmen interviewed during our research said that while the cost of the loans can be high, most consumers are aware of these costs because typically they are clearly presented by lenders at the outset. This is echoed by other research: a 2013 Citizens Advice survey of payday borrowers found that eight in ten were clear about the total repayment cost of the loan.[47]

table 14: reasons why consumers had complained to the ombudsman service about payday loans

	main feature of complaint	all features of complaint
high charges	**3%** (10)	**16%** (56)
high interest rates	**4%** (15)	**12%** (44)

Moreover, research conducted by the Personal Finance Research Centre at the University of Bristol suggests that only a minority of payday loan borrowers look at APRs. Instead, most look at the total cost of the loan – including fees and charges. But it also found borrowers were insensitive to the price charged. When asked if they would have still taken the loan if it had cost more, 44% of online payday loan borrowers said yes, rising to 56% of high street payday loan customers.[48]

Complaints about interest and charges in the sample we reviewed largely related to the interest and charges applied once a borrower missed a repayment (default charges) and the fees applied when a CPA didn't work due to insufficient funds in a borrower's bank account (debit attempt fees). Complaints about excessive interest rates were similarly more likely to come once a borrower was in significant difficulties and struggling to repay – so their debt was escalating.

> " The application of high charges and the frequency of those charges can come as a shock. When you've missed a payment you know you're going to get hit, but you're not necessarily aware of how hard."
>
> **Stephen Cooper, ombudsman**

As many as a third of payday loans might be repaid late or not at all, meaning that many consumers are incurring late charges.[49] And yet default fees can come as a shock to the consumer. Research by the former Competition Commission (now the CMA) found that "customers tend to become aware of rollover or penalty charges only when they incurred them."[50]

One explanation, according to a further CMA report, could be that online providers do not always present late payment or default fees on the same internet page that shows other costs and charges. It concluded: "This implies that customers have to make an additional effort in order to find out information on these fees."[51]

As noted earlier, the FCA has now published proposals to cap – from January 2015 – the total amount that high-cost short-term credit lenders can charge. There are three elements to the FCA's proposed approach. In addition to a cap on total costs (100% of the amount borrowed, applying to all interest, fees and charges), there will be a daily limit on the interest and charges that can be applied (0.8% of the amount borrowed), and a maximum limit of £15 on default fees. [52]

In the following case study drawn from our review of complaints, an ombudsman ruled that the lender had not treated the consumer 'fairly or reasonably' in its application of a succession of high charges.

case study

Unfair application of charges ramps up consumer's debt

Mr H took a £100 loan but got into financial difficulty and was unable to repay. The lender levied an immediate £25 default charge. Just days later a further default charge was issued. Over the course of three months numerous debit attempt fees were also charged, totalling £400. Mr H informed the lender of his difficulties but it continued to apply charges and interest. It also refused to give Mr H a breakdown of what charges it had applied. The ombudsman ruled that the lender had not helped the customer even when it knew of his difficulties. It had continued to apply interest and charges and to pursue debt collection activity – dramatically increasing the size of Mr H's debt and causing him distress. The complaint was upheld. Most of the charges and interest were refunded, and Mr H was awarded £150 in compensation for trouble and upset. The lender was also required to inform credit reference agencies that the debt was settled, reflecting what the loan balance would have been had interest and charges been frozen.

Looking at our sample of complaints, we found that vulnerable consumers and those in hardship were more likely to complain about high charges and interest.[53] Almost a quarter (23%) of vulnerable consumers in our sampled cases complained about high charges and almost a fifth (19%) complained about high interest rates. This compares to 8% and 5% respectively among those consumers where factors of vulnerability were not evident in the case file.[54]

One possible explanation for this disparity is likely to be that the charges relate to defaults and unsuccessful debit attempts. The debt advice charity StepChange, which last year recorded an 82% increase in consumers seeking its help with payday loan debts, commented earlier this year that: "StepChange continues to see numerous cases in which debts are excessively inflated through the application of interest and charges. In one case the charity helped a man whose £200 debt grew to £1,851 in just three months".[55] We saw similar instances in our review of complaints where at the point at which a consumer hit repayment problems, the application of charges – sometimes levied frequently over a short period of time – significantly increased the consumer's debt, further impacting their ability to repay.

The case study below presents one such example, where a consumer's original debt increased tenfold due to the application of a range of fees and charges.

case study

£100 initial loan grows to more than £1,000 due to charges and interest

Miss O was in financial difficulties and unable to repay her loan on the due date. Over a five-month period, a combination of default charges, debit attempt fees, interest, and a debt recovery fee acted to increase the debt from £100 to £1,000. After intervention by Citizen's Advice, the lender agreed to a final settlement of £450 via a repayment plan. Miss O felt that this was still unfair. But the ombudsman service adjudicator was unable to uphold her complaint as Miss O did not respond to requests for additional evidence and information to support her case.

> "High APRs aren't the foremost of consumers' concerns. Their main worries are 'will I get the money' and 'when will I get it'? If you don't have a choice about how and where you borrow, you're less likely to be complaining about the cost."
>
> **Dan, adjudicator**

chapter 10

the experience of vulnerable consumers

the experience of vulnerable consumers

A large proportion of the consumers who brought payday loan complaints to the Financial Ombudsman Service could be considered 'vulnerable'. Consumers are not obliged to tell the ombudsman service about their personal circumstances, and our research did not use a specific criteria or measure of vulnerability. But evidence of vulnerability was often visible within consumers' case files. This chapter takes a closer look at their experience.

snapshot

- More than half of all the reviewed complaints had at least one background factor which meant the consumer could be considered 'vulnerable'. These included financial hardship, unemployment, disability, acute illness and mental health issues.
- The most common reasons for complaint among vulnerable consumers differed from the remainder of the sample. The leading reason for complaint was lenders ignoring or not accepting debt repayment plans.
- Businesses' treatment of vulnerable consumers was mixed. But where bad practice did occur, it could cause a rapid escalation of the consumer's debt problem.
- Vulnerable consumers were more likely to have rolled over and topped up their loan. It was also more likely that their loan debt was outstanding at the point the consumer brought the complaint to the ombudsman service.

financial hardship

According to research undertaken by the former Competition Commission, more than a third of payday loan borrowers are considered to be on a 'low income', with a net household income of £18,000 or less.[56] More than half have had debt problems in the past five years.[57] And two-fifths (39%) are reported to have no access to alternative sources of credit.[58]

In that context, it was not surprising to find financial hardship featuring prominently in our research: 42% of the complaints we reviewed centred on consumers struggling with their finances. In total, more than half of the sample – 52% of the reviewed complaints – contained evidence that the consumer was in a 'vulnerable' situation, which we took to incorporate financial hardship and a range of other possible indicators, such as acute illness, unemployment and addiction.

Chapter 3 outlined the information we were able to glean on how long the payday loans taken out by the consumers in our sample had been running. We found that vulnerable consumers were much more likely than the rest of the sample to have an ongoing loan at the point of complaint to the ombudsman (67% against 38%). Clearly, as a service we see cases where something has both gone wrong and a business has been unable to resolve the issue to a consumer's satisfaction. As such, the proportion of outstanding loans might be expected to be high. But as the comparison above suggests, it is also likely to be an indicator of loan repayment problems.

reasons for complaint

The features of the complaints brought by vulnerable consumers also tended to differ – sometimes strikingly so – from those in the remainder of the sample.

As shown in table 15, the most common feature of complaints brought by vulnerable consumers were problems agreeing a debt repayment plan with a lender.[59]

In stark contrast, only one per cent of the sample group who did not fall in the vulnerable category complained about a lender failing to accept or respect a debt repayment plan.

Further mismatches can be seen in the respective prominence of complaints about high charges (23% against 8%) and unaffordability (14% against 1%).

table 15: why had consumers complained?

	vulnerable group		remainder	
problem with debt repayment plan	**34%**	(63)	**1%**	(2)
poor customer service	**25%**	(46)	**16%**	(27)
aggressive chasing for debt	**23%**	(43)	**13%**	(21)
high charges	**23%**	(43)	**8%**	(13)
unexpected/unauthorised taking of funds	**23%**	(42)	**15%**	(26)
damage to credit record	**19%**	(36)	**29%**	(49)
high interest rates	**19%**	(36)	**5%**	(8)
unaffordability	**14%**	(25)	**1%**	(1)
poor administration	**11%**	(20)	**29%**	(49)
rollovers	**7%**	(13)	**2%**	(4)
allegation of fraud	**4%**	(8)	**30%**	(50)
misleading information	**3%**	(5)	**8%**	(13)
application for other credit rejected	**2%**	(4)	**4%**	(6)
other	**10%**	(18)	**14%**	(25)

base: 353 complaints: 185 complaint cases with a background feature of vulnerability, 168 complaint cases with no obvious indicator of vulnerability. The results show all aspects of the complaint – that is to say the main reason plus any additional reasons cited by the consumer or apparent from the file.

top 5 features of complaints:

vulnerable customers

- lender ignored/did not accept repayment plan
- poor customer service
- aggressive chasing for debt
- high charges
- unexpected/unauthorised taking of funds

remainder of the sample

- allegation of fraud
- damage to credit record
- poor administration
- poor customer service
- unexpected/unauthorised taking of funds

“Payday loans are not the first port of call for most people. There is something in the type of lending being offered – short-term and high-cost – that in itself suggests borrowers have a background of financial hardship or could be excluded from mainstream credit.”

Mark Hollands, ombudsman

The sampled cases with no obvious indicator of vulnerability were much more likely to feature complaints that the consumer had not taken out the loan, damage inflicted to their credit record, and poor administration. Unhappiness at poor customer service and the unexpected taking of funds was apparent across the sample.

The case studies below illustrate examples drawn from our sample of typical complaints from vulnerable consumers about debt repayment plans and the unauthorised taking of funds.

case study

lender ignored attempts to set up a repayment plan

Following redundancy, Mr T hit financial difficulties and contacted the lender to ask it to freeze interest and charges, and to arrange a suitable repayment plan. Mr T said these requests were ignored. He complained that he was encouraged to roll over the loan as a way of dealing with the problem. Although Mr T had told the lender about his difficulties on four occasions before the loan repayment date, the lender did not respond, and Mr T defaulted. Mr T's complaint was upheld by the ombudsman service, and the lender was ordered to reduce the outstanding balance to remove interest and charges applied after Mr T had informed it lender of his financial difficulties. £100 was awarded in recognition of the trouble and upset caused by the lender's failure to reply to the initial correspondence and ignoring Mr T's emails requesting help.

case study

lender's misuse of the CPA on a customer in hardship

Mr N was having difficulty repaying a loan so he set up a repayment plan with his lender. But this too was soon unaffordable and Mr N missed a repayment. The lender then started to take funds from Mr N's bank account through the CPA. This pushed Mr N further into financial hardship and left him struggling to pay essential bills. When Mr N made contact with the lender he found them unhelpful and rude. Mr N's complaint was upheld. The adjudicator ruled that the lender had not exercised any forbearance and had misused the CPA. The ombudsman service made an award in compensation for the trouble and upset caused to Mr N, and the lender was required to help set up an affordable repayment plan for him.

the 'debt spiral'

As a wide range of research has demonstrated, household finances can be fragile.[60] And it was evident from the complaint cases we reviewed just how quickly things can go wrong for payday loan borrowers. It was not uncommon for a consumer's financial situation to be so precarious that a change in circumstances, often only a short-term change such as a temporary drop in earnings or a hospital stay, could lead to an immediate and acute problem in their ability to repay their loan.

Repayment problems with payday loans are quickly exacerbated because of the high charges and interest applied on the debt, particularly when borrowers fall behind with their contractual repayments. For example, almost all lenders charge an immediate late payment fee or default charge on the first day a repayment is missed. These fees are currently believed to range in size across the market from £8 to £30,[61] though will clearly be affected by the new charging rules being introduced by the FCA from January next year.

We repeatedly saw instances where a rapid succession of high charges meant that once a borrower hit financial problems, their debt had the potential to escalate quickly. And with many consumers having more than one loan, the problem is often magnified. The debt charity StepChange, which helped more than 66,000 consumers with payday loan debt problems in 2013, found that as many as one borrower in five has five or more payday loans running concurrently.

It was also clear from the complaints we reviewed that many borrowers had taken out one payday loan to repay another. Four in ten consumers in the vulnerable group we identified had had a previous payday loan. This figure fell to just 27% among consumers whose complaints did not show obvious evidence of vulnerability. Consumers can clearly get stuck on a payday loan treadmill.[62]

The following case study illustrates the precarious nature of one consumer's financial situation, in a scenario that was not uncommon in our vulnerable group.

case study

impact of a short illness on consumer's ability to repay his payday loan

Mr E had taken out a significant number of loans over an 18-month period with the same lender. He had been working and the loans had all been successfully paid on time. But Mr E was then unwell and was admitted to hospital for a number of weeks, meaning his income stopped and he was unable to repay his loan on the required date. Despite informing the lender of this change in circumstances in advance of the repayment date, and requesting that his debt be frozen, the lender applied default charges and continued to levy interest. This caused Mr E's debt to increase and he was unable to repay the balance. The loan grew to eight times its original size. Mr E complained to the ombudsman about the charges. He had tried to set up a repayment plan with the lender, but without success. The complaint was upheld. The lender agreed to reduce the outstanding balance and a set up a repayment plan.

table 16a: did the consumer's payday loan 'roll over'?

yes	**28%**	(77)
no	**52%**	(144)
unknown/not applicable	**21%**	(57)

base: 278 complaints, omitting cases incorporating suspicions or allegations of fraud.

table 16b: if the consumer's payday loan did roll over, how many times did it do so?

1	**32%** (25)
2	**16%** (12)
3	**18%** (14)
4	**5%** (4)
5	**6%** (5)
6	**3%** (2)
7	**1%** (1)
8	**1%** (1)
9	**1%** (1)
10	**1%** (1)
more than 10	**4%** (3)
unknown	**10%** (8)

base: 77 cases in which the consumer's loan did roll over.

rollovers and top-ups

rollovers

The majority of payday lenders allow borrowers to roll over or defer their loan beyond its original repayment date. With a rollover the borrower pays the interest – or finance charge – on the loan but carries over the principal loan amount, extending it typically for one month. The terms and conditions of the loan remain the same and typically a flat-rate fee is charged for the process.

As shown in table 16a, we found evidence in almost three in ten of the complaints we reviewed (28%) – excluding those complaints featuring an allegation of fraud – that the consumer's loan had been rolled over. Of those that had rolled over, about one in three loans were rolled over once but two-fifths (42%) had rolled over three times or more, as shown in table 16b.

"When things go wrong a small loan can quickly grow to an eye-watering debt in a short space of time. High interest and charges can quickly push someone into a vicious spiral of debt."

Juliana Francis, senior ombudsman

Rollovers can be useful for consumers as they allow them to avoid default fees and damage to their credit file if they are struggling to meet the loan debt in full on the repayment date. But sometimes a rollover can be an early indicator of financial difficulties or a sign that the borrower may have a problem repaying the debt. And rollovers have raised other concerns. In its review of the market, the Office of Fair Trading, the former sector regulator, found that rollovers were key profit drivers for lenders, accounting for around 50% of revenue. It found that some businesses were deliberately encouraging borrowers to roll their loans over rather than repay.[63]

In many of the cases we reviewed, rolling over the loan caused the borrower greater financial problems as the increased fees and interest grew the total debt burden, as the following example illustrates.

case study

excessive rollovers exacerbate consumer's financial difficulties

The lender allowed Mrs L to roll over her loan more than 15 times. On each occasion a rollover or extension 'fee' was charged at £100, meaning the small initial loan grew significantly to more than £1,500. The business argued Mrs L had not informed it of her financial problems, but the adjudicator said the fact the consumer had extended the loan on so many occasions should have been a clear indicator that there was an underlying problem. The business did not offer Mrs L any other way of clearing the balance and did not refer her to debt charities. The complaint was upheld. The outstanding balance was removed and compensation was awarded.

FCA regulation of the payday sector, which began on 1 April 2014, now restricts rollovers. Lenders cannot allow a loan to roll over more than twice. This should help to prevent borrowers' debts from escalating to unmanageable levels. One ombudsman working in consumer credit believes that some desperate borrowers might try to find ways to extend their line of credit. He commented: "Some borrowers could transfer their debt elsewhere by borrowing from another payday lender – effectively rolling over, just with another company." The ombudsman service will monitor this area and alert the FCA to systemic breaches of its rules.

> "Often a rollover is an indicator that the borrower will struggle to repay the debt. It is delaying the inevitable. Unfortunately we sometimes see borrowers going to different payday lenders to get the funds to repay their previous loan."
>
> **Robert, adjudicator**

top-ups

A loan top-up is where the customer applies to borrow additional funds on top of their original or principal loan. But both debts – the principal loan and the top-up – will have the same repayment date – typically at the end of one month. In a similar way to rollovers, most lenders also charge a flat-rate fee to top up a loan.

The graphic opposite shows how rollovers and top-ups can increase the total cost of the original loan. For simplicity, we have chosen a straightforward example from the complaints we reviewed, incorporating a single top-up and rollover. We saw many others however, where multiple top-ups and rollovers quickly and significantly increased the consumer's debt.

Overall, we found that vulnerable consumers were almost twice as likely to have rolled over or topped up their loan, as figure 13 illustrates.

> "Time and again we see cases where the consumer is in difficulties but the business communicates poorly or applies its contract terms too rigidly. This means problems can soon escalate."
>
> **Stephen Cooper, ombudsman**

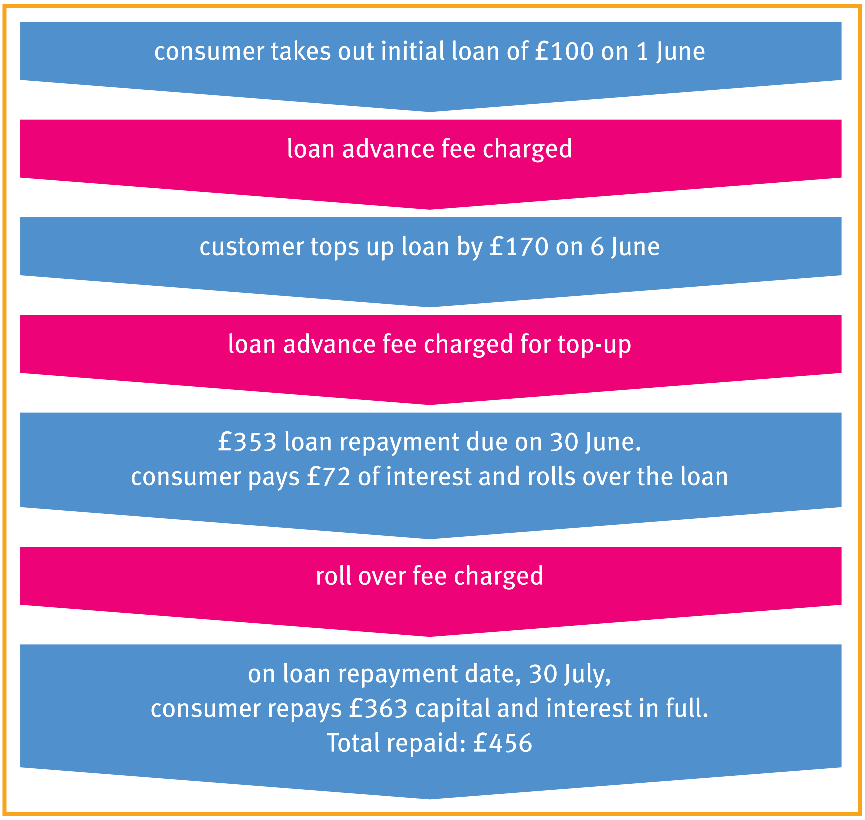


figure 13: loans that were rolled over or topped up

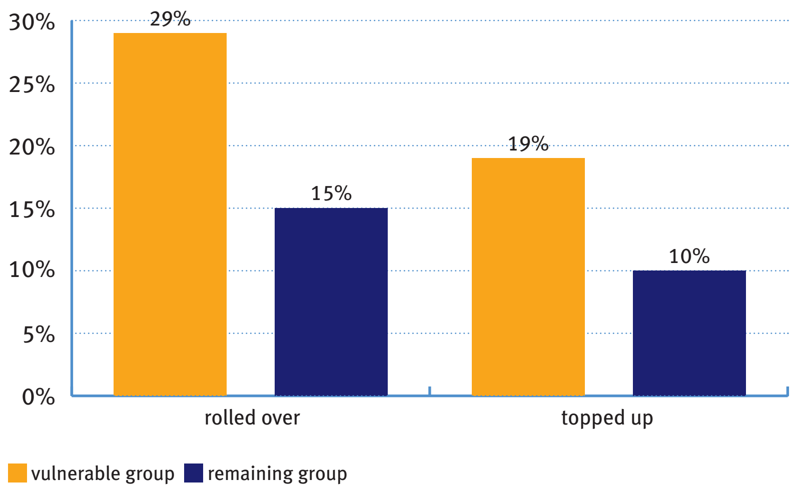


table 17: was the consumer's payday loan 'topped up'?

yes	**18%**	(50)
no	**64%**	(177)
unknown/not applicable	**18%**	(51)

base: 278 complaints, omitting cases incorporating suspicions or allegations of fraud.

business practice

Following intense political, regulatory and media pressure, the payday lending industry introduced a voluntary code of practice, known as the 'Good Practice Customer Charter', in November 2012. The Finance & Leasing Association, Consumer Finance Association, the Consumer Credit Trade Association and the British Cheque & Credit Association, trade bodies which represent 90% of the payday lending sector, are signed up to the Charter.

Our review of complaints, however, revealed a very mixed picture of business practice. There was evidence of both good and bad practice in almost equal measure. In the 'vulnerable' complaint cases, we found that 30% had observable characteristics of good practice by the business, such as freezing interest rates and charges, writing off or reducing part of the loan balance, or referring consumers to free debt advice services. But in 31% of cases the lender demonstrated poor practice, out of keeping with the Charter. And in the remaining 38% of cases, it was not possible to discern evidence either way.[64]

payday lending industry customer charter

If you are having problems repaying your loan we will:

- deal with cases of financial difficulty sympathetically and positively and do what we can to help you manage what you owe.
- freeze interest and charges if you make repayments under a reasonable repayment plan or after a maximum of 60 days of non-payment.
- tell you about free, independent debt-counselling organisations who can help you.

The qualitative interviews we undertook with ombudsmen and adjudicators as part of our research suggests there is widespread poor practice by lenders in their treatment of those in hardship. Clearly, it is worth acknowledging again that the ombudsman service deals with entrenched complaints. We might be expected to see the worst end of the market, handling instances where the borrower-lender relationship has broken down.

But other research does tend to corroborate our finding that some lenders do not always treat struggling borrowers sympathetically.[65] During its regulation of the industry, for example, the Office of Fair Trading found that attitudes to forbearance varied and that only one fifth of the lenders had specialist teams in place to deal with financial hardship.[66]

One ombudsman described some businesses as "intransigent" and unable to look at the personal stories behind the problems. He said he saw many cases where lenders had not applied their code of practice. Another described some businesses as having a "cavalier attitude" towards those in hardship, commenting that: "Businesses are quick to point to the contract and rule book when it suits them. But then they take free rein when it comes to clawing back cash, regardless of a person's financial situation and ability to pay."

forbearance

However, ombudsmen and adjudicators also pointed out that in many cases businesses do adhere to the customer charter, and our sample evidenced examples of good practice by lenders dealing sympathetically with borrowers in hardship or in vulnerable situations, and showing forbearance.

Sometimes, consumers can exacerbate their own debt problem by not tackling the issue early enough. Debt advisers reported to the Office of Fair Trading that, on average, consumers had rolled over their loan four times before seeking independent help.[67] One ombudsman described some borrowers as "burying their heads in the sand" about their debt problems. He said: "Months, or even years, can roll by and the consumer has done nothing to get in contact with the lender."

> "Some lenders are unaware of the rules or guidance that should be followed when it comes to dealing with vulnerable consumers."
>
> **Mark Hollands, ombudsman**

A reluctance to deal with debt problems, or to negotiate with lenders, can make the issue worse for borrowers, as the next case study from our sample shows.

case study

proactive lender tries to help a customer with debt problems

Miss A took out a payday loan but, due to a change in her circumstances, was unable to pay it back. She asked the lender if she could enter into a debt repayment plan which the business accepted – freezing all interest and charges. The lender also referred the consumer to a free debt charity. Miss A made no payment. She then contacted the lender to negotiate a reduced monthly repayment. The lender agreed to the reduced offer but the repayment plan was not honoured by Miss A. Miss A complained and said there had been a lack of assistance from the business. The adjudicator did not uphold the complaint and judged that the lender had not been unhelpful or inconsiderate of the consumer's financial difficulties.

Adjudicators told us during our review that for some consumers there is still a stigma attached to suffering serious debt problems and in using payday loans. They say this might explain why in some cases consumers seek help very late. One adjudicator said: "Sometimes a consumer has hidden loans from their partner or other family members. Eventually they've been found out, typically because the debt level is out of control."

There is also a well-established link between debt and depression. According to debt charity StepChange, at least half of those in debt feel anxious or depressed.[68] Research also suggests that people with debt and mental health problems often don't seek help for financial difficulties and don't disclose information about such illnesses to creditors due to embarrassment or fear of not being believed.[69]

In some of the complaints we reviewed, such as the following case study example, the consumer appeared to be evasive, making it extremely difficult for the lender to understand the extent of their personal situation.

> "People are often embarrassed to be using payday loans, although for many consumers it is their only option."
>
> **Robert, adjudicator**

case study

consumer makes little contact with his lender over a period of many months

Mr Y took out a large loan but did not repay on the due date. No contact was made with the lender for many months. After Mr Y did eventually make contact, the business suppressed interest and charges.

But it was particularly difficult for the lender to set up an agreed repayment plan with the consumer and, when arrangements were put in place, Mr Y did not stick to them. The consumer complained about adverse markers on his credit file and said the business should have been more helpful.

The adjudicator did not uphold the complaint and considered that the settlement offer the business had already made was fair and reasonable. He also said the credit file information was correct and an accurate reflection of Mr Y's payment history.

chapter 11

referral rights and post-decision contact

referral rights and post-decision contact

The way in which businesses treat their customers during complaints can be indicative of the value they place on customer service. A central part of the official complaints procedure is the 'final response letter', and our review uncovered serious problems with misleading information or letters routinely not issued. In this chapter we put the spotlight on business practice and firms' proactivity during complaints. While there are plenty of examples of good practice, most payday lenders must do more to improve complaints handling.

snapshot

- More than half of reviewed complaints did not have a final response letter in the complaint file. It either had not been issued or was not available.
- In four in ten complaints, lenders had given consumers their full referral rights – and within the eight-week time frame.
- In almost a fifth of upheld complaints, the consumer had to contact the ombudsman service after the resolution of their complaint because the business had either not paid redress or had failed to correct the information on their credit file.

final response letters

When any regulated financial services business receives a complaint – or any expression of dissatisfaction – from a customer, which it is unable to resolve by the end of the next business day, it must send its response within eight weeks. Whether the business is able to offer a solution, rejects the complaint, or even if it has been unable to investigate within the time frame, it must send written acknowledgement to the consumer.

final response within eight weeks

If the business cannot resolve the complaint by the end of eight weeks it must send the complainant:

A copy of the Financial Ombudsman Service's standard explanatory leaflet, and inform the complainant that if he remains dissatisfied with the business' response, he may now refer his complaint to the Financial Ombudsman Service and must do so within six months.

Alternatively, it must send:

A written response which: (a) explains why it is not in a position to make a final response and indicates when it expects to be able to provide one; (b) informs the complainant that he may now refer the complaint to the Financial Ombudsman Service; *and* (c) encloses a copy of the Financial Ombudsman Service standard explanatory leaflet.

DISP 1.6.2 Financial Conduct Authority

Most importantly this 'final response letter' must include 'referral rights'. This will clearly explain to the consumer that they have the right – whatever the business's decision on their complaint – to escalate their case within six months to the Financial Ombudsman Service for an independent decision. This legal minimum requirement is covered under the Financial Conduct Authority's Dispute Resolution rules – known as 'DISP'.

The full guidance from the FCA handbook for businesses is shown on page 60.

In just under half of the complaints we reviewed, the consumer had been given full referral rights within the eight-week time frame permitted. In the remaining half of cases there was a mixed picture of practice. In some cases referral rights had not been given at all, or were incomplete or misleading. Other letters were issued outside the allotted eight-week timeframe – in breach of FCA rules. Worse, in a significant proportion of complaints, a final response letter was not issued at all, and in other cases it was not available within the case file.

The findings of our latest review echo previous ombudsman service research into the provision of referral rights within payday loan complaints. [70] Adjudicators and ombudsmen feel the issue is largely due to businesses' inexperience and a lack of awareness of the rules, rather than a deliberate attempt to prevent consumer complaints coming to the ombudsman. An adjudicator told us: "Lenders seem unsure of their obligations rather than wilfully contravening the rules. Compliance probably isn't a key focus for some of these businesses, many of which are start-ups and very small."[71]

Not all of the practice we observed was poor. Among the complaints reviewed in our sample, for example, some firms issued full referral rights on time in a high proportion of cases. This compares to some other lenders who met this standard in fewer than 20% of complaints.

Incomplete or absent referral rights are a problem. If consumers are not given full referral rights by businesses, many will not know they can bring their case to the ombudsman service where their complaint will be given an independent hearing. There are also risks for firms themselves. The final response letter sets the clock ticking on a complaint – after six months the case will be time-barred and the ombudsman service will no longer be able to consider it. If a business fails to inform the consumer of their referral rights, the complaint remains 'live' and that consumer could choose to bring the complaint to the ombudsman at any point in the future.

what we expect to see

Here are two examples of final response letters drawn from our sample of complaints. Both businesses had investigated and set out their conclusions in the final response letters. They both comply with DISP and set out referral rights to the consumer along with the six-month time scale.

Please note that according to our Complaints Procedure, this is our final response. If you are unhappy with it, you may refer your complaint to the Financial Ombudsman Service.

You need to do this within six months of the date of this letter. For more information please visit

www.financial-ombudsman.org.uk/publications/consumer-leaflet

The address of the Financial Ombudsman Service is:

Exchange Tower London E14 9SR

Once again we apologise for the inconvenience you have been caused and hope that you will find the points above as a fair resolution to your complaint.

final response

If you remain unhappy with my reply I am enclosing a leaflet about the Financial Ombudsman Service.

Should you choose to contact them, you will need to do so within six months from the date of this letter, enclosing a copy of my response, which they will need for their investigation.

Please do not hesitate to contact me should you require any further assistance. You can email me on ...

misleading final response letters

But we also uncovered worrying practice. Examples included lenders not issuing a final response letter at all, or sending the letter late – after eight weeks had elapsed since the complaint. Moreover, about one in ten of the final response letters we reviewed had either incomplete information (for example a failure to mention the six-month time limit for bringing a complaint to the ombudsman), or were misleading. Particular examples of the latter were those final response letters which guided consumers towards alternative complaints procedures.

The excerpt on page 63 from a final response letter illustrates just such an example, referring the consumer to the complaints procedure of the lender's trade body – the British Cheque and Credit Association (BCCA) – and not making it clear that the consumer could take their complaint straight to the ombudsman service. In this particular case we raised our concerns with both the firm and the FCA to ensure best practice.

Some of the final response letters we reviewed were so poor and lacking in clarity that the consumer or adjudicator had to query with the business whether it was in fact their final response. It is important to know exactly when a final response is issued as this letter marks the start of the six-month window for cases to be considered at the ombudsman service.

In other final responses, businesses referred to previous complaints against them that had not been upheld by the ombudsman service. Because each complaint is individual, and is assessed on its own merits, it is extremely misleading to refer to past cases and imply that the ombudsman will arrive at the same outcome, and risks deterring consumers from pursuing their complaint.

One lender in our sample even referred to the Financial Ombudsman Service as 'colleagues'. While this reference was not made in a final response letter, it was included in the business's correspondence to the consumer during their complaint. Again, adjudicators and ombudsmen say this is misleading. They point out it is essential for consumer trust in the process for consumers to understand that the ombudsman service is independent and impartial and that their complaint will have a fair hearing.

Please note that under the terms of our complaints procedure this is our final response. If you are dissatisfied with the way we have handled your complaint, you can go to stage 2 of the procedure by referring your complaint to the BCCA which is our Trade Association and acts on our behalf.

The BCCA will investigate your complaint and will provide you with a final response within four weeks of receiving notification of your continuing dissatisfaction.

We will regard your complaint as closed if the BCCA does not receive a reply from you within eight weeks of our final response.

If you are dissatisfied with the final response from the BCCA you can ask the Financial Ombudsman Service for an independent review. The BCCA will enclose a leaflet from the ombudsman in their final response letter to assist you if you decide to pursue this further course of action. You should contact the Financial Ombudsman Service within six months of receiving the final response from the BCCA.

adjudicator's opinion to the business

I have now reviewed the email correspondence which the business sent to Ms C during her complaint.

In an email sent to Ms C it referred to the OFT* and the Financial Ombudsman Service as its colleagues.

I feel the use of the word 'colleagues' is misleading as it gives the impression that we work with businesses and may cause Ms C to feel any assessment of her complaint may be biased.

This is not the case. We are an independent complaints organisation and the OFT is the regulator.

** The FCA assumed responsibility for the regulation of consumer credit from the OFT in April 2014.*

While some lenders clearly act responsibly when faced with a complaint, the failure of parts of the market to deal with complaints correctly is not just bad news for the consumer, but bad news for the industry. Previous internal research we have undertaken had identified the inconsistent quality of payday lenders' final response letters and their provision of referral rights as a problem. Our latest review has underlined it. We will be keeping a close eye on this issue and will share examples of continuing poor practice with the regulator.

post-decision contact

The ombudsman service's decisions are based on what we believe is fair and reasonable in the circumstances of each individual case. We take into account the law, rules, codes and good practice that applied at the time of the event complained about. We look at all the relevant facts and arguments, ask both the business and the consumer for their views, and listen to each side of the story.

After drawing together all the evidence, we will let both parties know what we think – on the balance of probability – is the most likely version of events. In most cases, both the consumer and the business accept our adjudicator's view and the complaint is settled.

In some instances, however, consumers whose complaint we have upheld contact us to say that the business has not yet taken the action we have recommended. As table 18 shows, in almost a fifth of the upheld complaints we reviewed, the consumer had to contact the ombudsman service again[72] because the business had not followed through on the ombudsman's decision – typically by not having paid the redress owed or by not having amended entries on a consumer's credit record as directed.

table 18: has the consumer contacted the ombudsman post-decision about unpaid redress (at least one month after the decision)?

yes	**18%**	(38)
no	**82%**	(177)

base: 215 upheld complaints, including cases incorporating suspicions or allegations of fraud. The 'yes' value includes instances of consumers contacting the ombudsman about a lender's failure to amend entries on the consumer's credit record.

chapter 12

live issues

The findings of this report are based on complaints against payday lenders which the ombudsman service dealt with in 2013/14. But this is a fast-paced market and products and business practice are changing. A number of issues emerged during the interviews with ombudsmen and adjudicators which did not feature strongly in the casework review. This chapter highlights some of those issues and gives a snapshot of where the market is now – and where it might be heading.

affordability at the point of sale

The unaffordability of a loan at the point of sale is a growing feature of payday loan complaints, according to ombudsman service adjudicators. The issue did feature in the complaints we reviewed but was not a prominent theme overall (discernible in 7% of cases when all features of the complaint were taken into account).

This is perhaps surprising given the extent of media coverage and consumer campaigning on the subject. The debt charity StepChange, for example, is just one of the bodies that has raised concerns about affordability and irresponsible lending. It recently found consumers with payday loans seeking its help had average debts of £1,647, against these borrowers' average net monthly income of £1,381.[73]

And a survey by the Personal Finance Research Centre at the University of Bristol found that although the majority of consumers were asked for information to help the lender assess affordability, only a minority of businesses (9% of online lenders) asked for physical proof of income, such as bank statements.[74]

Ombudsmen say unaffordability has not played a significant part in the payday complaints received to date mainly because of the way consumers frame their complaint. One commented: "It feels unlikely that a consumer would say 'I couldn't afford this loan, they should not have given it to me', particularly when they are in a difficult financial situation and desperately need the money. But when you scratch beneath the surface of many complaints affordability is often found to be the root cause of the problem."

One explanation for the growing visibility of unaffordability complaints could be greater consumer awareness of a lender's obligation to ensure a loan is affordable at the outset. It is something the Financial Conduct Authority made mandatory when it took over regulation of consumer credit in April 2014. And the forthcoming cap on the total cost of credit, due to be brought in by the FCA from January 2015, has also had extensive media coverage. This could have had the effect of boosting complaints about loan costs and affordability.

> "Some businesses don't make enough effort to check if loans are affordable, and some consumers don't realise they are required to."
>
> **Stephen Cooper, ombudsman**

The following case study from our review sample is a prime example of where a lender had not applied sufficient checks on affordability.

case study

Initial loan advanced was almost as big as the consumer's income

Mrs R complained on behalf of her son because a loan had been issued which she felt was unaffordable. The lender had given the borrower a loan which was almost equal to his total net monthly income. This was despite the borrower declaring his income on the application form. The borrower had got in to difficulties and interest and charges had more than doubled the outstanding balance. It had been referred to a debt collector prior to the complaint. The case was upheld. The adjudicator said he had 'significant concerns' about the adequacy of the lender's assessment of the borrower's ability to repay.

Better data sharing, combined with more rigorous regulation, should improve the effectiveness of lenders' affordability assessments. Russell Hamblin-Boone, chief executive of the Consumer Finance Association, one of the trade bodies representing the payday lending industry, has said of Callcredit's real-time credit reporting database: "We support real-time credit checks as they will help lenders not only to identify customers who can afford to repay a loan but also those who apply for credit in the full knowledge that they can't afford it".[75]

product innovation

Ombudsmen and adjudicators report a shift in emphasis by some payday lenders away from the traditional 30-day payday model into different products, such as short-term (two, three or six-month) structured loans or running credit accounts, sometimes known as flexible or 'flex accounts', possibly in response to new FCA rules capping rollovers. As one adjudicator commented, "Rollovers are a big source of revenue for lenders. If this dries up it stands to reason they'll want to adapt the product or look to offer something different". But the extent to which this evolution will spread across the market – if at all – is inherently uncertain.

instalment loans

Wonga, the biggest payday loan brand in the UK with an estimated 20% to 30% share of market revenue,[76] started trialling six-month instalment loans in a pilot scheme offered to existing customers earlier this year.[77] And US-owned lender SRC Transatlantic Ltd told the Competition and Markets Authority during its market investigation that the US market had 'evolved towards instalment products' in recent years.[78]

But other providers may not follow. Another payday lender told the CMA that regulatory change and uncertainty were likely to stifle innovation and that firms were "putting plans to launch new products on hold".[79] Other independent analysis suggests a cap on the total cost of credit will cause some lenders, particularly smaller businesses, to exit the market altogether.[80]

> " More lenders are offering short-term structured loans and running accounts with an ongoing line of credit. This is possibly in response to tighter FCA rules on rollovers."
>
> **Robert, adjudicator**

flexible accounts

With a 'flex' or running credit account the consumer takes a loan with flexible repayment terms. The loan operates more like a credit card than a loan. Typically there is a minimum monthly repayment required.

Crucially, because it is a running account with no end date, a lender can set the minimum payment to cover just the interest and a small proportion of the balance (typically about 2% of the principal loan). The loan then continues from month to month with the same terms and conditions.

One adjudicator said that "it is the same as deferring or rolling over the loan in all but name. The consumer can end up repaying only the interest each month – making just a small dent or never paying down the original capital of the loan".

Complaints about this type of flexible account were visible in our study in small number. But adjudicators expect complaints in this area to grow. One of the reasons cited by adjudicators is the increased complexity of the product. In the recent complaint to the ombudsman featured in the case study on the opposite page (which is not drawn from our review sample but included as an illustrative example), the consumer was unaware that by only paying the minimum repayment required each month they would never pay off the principal loan.

case study

confusion over minimum monthly repayments meant loan did not reduce

Mr D argued that the structure of his loan – a flexible running account – was misleading. The initial loan agreement had given an example of monthly repayments but this was only the minimum repayment required and it only covered the interest owed. It meant Mr D had been paying only the interest on the debt each month. Despite having the account for more than two years and paying hundreds of pounds in interest, the original loan amount had never been paid off. At first the lender argued the terms were clear but after the ombudsman service's intervention it agreed the loan documents at the outset had been misleading. The complaint was upheld. The lender was ordered to refund some of the overpaid interest and close the account.

claims management companies

Claims management companies (CMCs) will naturally look to different product areas to drive new business, especially as the volume of payment protection insurance (PPI) cases starts to decline. There has been speculation that payday loan borrowers could be a source of new complaints.

Adjudicators and ombudsmen have seen a small number of complaints brought by one CMC. But to date the caseload driven by this form of representation has been small. Nevertheless, adjudicators and ombudsmen report that some payday lenders believe that more CMCs are set to try their hand in this market.

So far, ombudsmen feel lenders' predictions should be less firm. One said: "We see very little activity from CMCs in payday loans. It isn't usually worth their while as the margins are low compared to PPI and packaged bank accounts, and there is quite a bit of work involved researching affordability cases." That said, potential CMC interest will linger – particularly as PPI complaints fall away. It could be that CMC activity in payday loans has yet to filter through in the cases seen at the ombudsman service.

credit broking

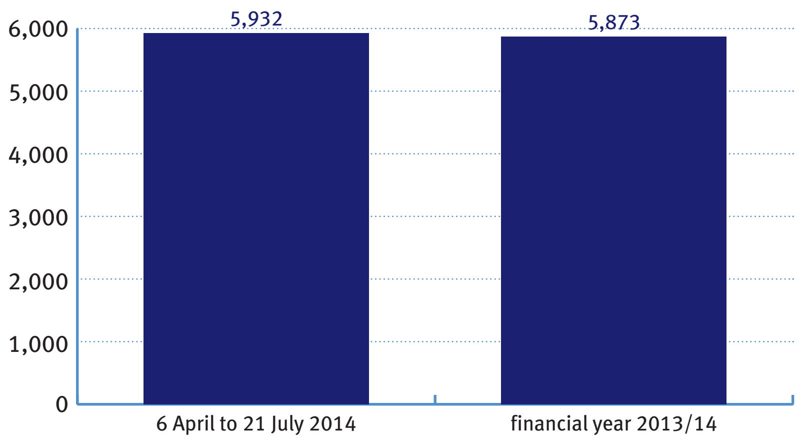
The Competition and Markets Authority's market investigation recently found that a "substantial proportion" of online payday lending customers use intermediaries – such as credit brokers – to apply for a loan, yet many consumers are unaware of the nature of the service with which they are being provided.[81] Many consumers assume that the broker is 'shopping around' on their behalf to find the best deal, when in fact the broker or lead generator auctions the customer's application to a panel of lenders – selling to the business that is willing to pay the most.

The ombudsman service has seen a significant increase in the volume of calls from consumers about problems they have experienced with credit broking services. In the 2013/14 financial year we received 5,873 enquiries from consumers about credit broking. Just over three months into the new financial year[82] we had already received 5,932 enquiries, exceeding the total for the whole of the previous year.

Figure 14 relates to all types of credit broking enquiries handled by the ombudsman service, but a high proportion relate to broking services connected to payday loans. A common feature of the calls we receive is for consumers to have paid a significant up-front fee to a broker, for example £70, as they think this is the only way to get a loan they need. Sometimes the broker arranges a payday loan – usually through a lender who would have lent the money to the consumer without any upfront fee had the consumer contacted them directly. But often the consumer does not end up with any loan at all, and in either scenario they have lost the £70. In many of the enquiries we have handled, the consumer was not even told about the fee, and merely gave their bank details to the broker who requested them "for verification", and only later found out money was taken.

In the most worrying examples, the broker which took the initial money from the consumer appears to be selling on the consumers' data to other brokers, which then also levy their own fees. Consumers have also expressed anger at harassment by phone and text message by various brokers and lenders as a result of their initial contact with a broker.

figure 14: credit broking enquiries



Despite the high volume of credit broking enquiries, very few (approximately 6%) convert into complaints. Part of the reason for the low complaint conversion rate is that the majority of businesses return or refund the fee charged when contacted on the consumer's behalf by the ombudsman service. The uphold rate for the credit broking complaints the ombudsman service does resolve is high, at 71%. Again, in the complaints that are not upheld, this is often because the business has already refunded the fee the consumer has paid, or has offered to refund the fee.

Due to the sheer volume of consumer enquiries we are receiving, and the nature of some of the business practice we are seeing, this is an issue we are monitoring closely.

> "With tightened affordability checks, the cap on rollovers and soon a cap on the total cost of the loans, payday lenders are feeling the heat of greater regulatory attention. I'd expect to see some big changes in the industry. Only the strongest will survive."
>
> **Juliana Francis, senior ombudsman**

chapter 13

conclusions

13 conclusions

The complaints that we resolve at the ombudsman service give us a particular perspective on the financial services industry. While the volume of calls to our helpline allows us to tap into consumers' emerging worries, by the time worries crystallise into complaints we inevitably find ourselves dealing with issues that businesses and consumers could not resolve. Our service comes at the end of a process when complaints are often entrenched. This is as true of complaints about payday loans as it is about other financial products. That acknowledged, our review of payday lending complaints has generated useful insight for us to share with others – some expected, some not. This chapter summarises what we found.

Our review of consumer complaints into payday loans found many recurring and interlinked themes. Some of these were familiar. Complaints about lenders' use of continuous payment authorities, and complaints from consumers who say they did not take out the loan they were being chased to repay, are issues the ombudsman service has highlighted previously.[83] But some of what we found was less predictable.

> "Poor administration and customer care simply isn't acceptable."
>
> **Financial Ombudsman Service**

business practice

The prominence of complaints about poor business administration was unexpected, for example. Looking at the main reasons for consumers' complaints to the ombudsman, dissatisfaction with a lender's administrative processes was twice as significant as unhappiness over high charges and interest rates – an issue which tends to command far more political and media attention.

Poor customer service did not feature prominently among the main drivers of consumers' complaints about payday lending. This is not especially surprising. In the context of the issues many payday borrowers face, pursuing a complaint about poor standards of care, or plain rudeness during a phone call, may seem a lower order priority. But when all observable features of complaints were analysed, poor service shot up the table: only topped by damage to credit records as the most frequently-occurring issue.

The complaints we reviewed revealed repeated evidence of lenders displaying poor administration or demonstrating little concern for customer care, with standards routinely falling below a level that many would consider reasonable. This simply isn't acceptable.

what can businesses do?

- **End poor administration.** Lenders should not be causing their customers undue trouble and upset because of poor systems and process. Putting resources into improving this area should reap rewards in customer satisfaction.

culture change

The new regulatory regime for payday lenders introduced by the FCA will tackle notable abuses of the system. But addressing poor administration and poor customer service are things that the industry can do independently of regulatory intervention.

It is something we have seen in other areas of financial services. Major banks and insurers have had their reputations tarnished in the past over various misconduct issues, not least the mass mis-sale of payment protection insurance. Consumer trust and respect was dented even further following the credit crisis. But many financial businesses have attempted to address the problem, investing resources in customer service and changing the culture inside their own organisations to ensure the customer is put front and centre of the operation.[84] This consumer-focused approach could helpfully be applied more widely in the payday lending industry.[85]

what can businesses do?

- **Make customers central to the business.** If a customer feels the need to raise an issue with a business, the business can often stop dissatisfaction escalating by listening and trying to put things right early.

awareness of the help available from the ombudsman

In the context of the relatively small number of complaints we receive about payday lending compared to the number of loans issued, we are extremely concerned at what our review revealed about the consistency with which lenders appropriately flagged consumers' ultimate right to have their complaint independently heard. In fewer than half of the complaints that we reviewed could we be confident that consumers had been given the right information within the right timeframe.

This is an obvious worry: if consumers are not given full 'referral rights', many may not know that they can bring a complaint to the ombudsman.

Our findings here are consistent with an earlier internal review we conducted on this issue, and we have been talking with the industry to help improve practice. But firms' obligations are simple and clear. If businesses continue to fail to signpost consumers appropriately to the ombudsman service, we will refer them to the regulator. There must be no unnecessary barriers between consumers and their entitlement to have their complaint independently reviewed.

what can businesses do?

- **Make sure consumers know their rights.** Full 'referral rights' are still not being provided consistently. The ombudsman service is working with businesses to raise standards in final response letters and will continue to flag poor practice to the FCA.

vulnerable consumers

Many organisations, especially consumer-focused groups such as Which? and the debt advice charity StepChange, have repeatedly highlighted concerns about lenders' handling of vulnerable borrowers. Complaints about businesses' poor treatment of those experiencing financial hardship also featured strongly in our review. We uncovered a very mixed picture of good, satisfactory, unsatisfactory and – at the extreme end – appalling treatment of borrowers in difficulty.

We have highlighted examples of good practice in our report. But too often we saw cases of consumers in financial difficulty being treated unsympathetically. In almost one in five of the cases we reviewed, the consumer was complaining because they were struggling to repay and the lender had refused to accept their debt repayment plan. A similar proportion of cases featured a complaint about aggressive debt chasing. This is unacceptably high, and we know these issues are firmly on the regulator's radar.

what can businesses do?

- **Help vulnerable consumers.** Some consumers find themselves in considerable financial difficulty. It is in everyone's interest to work together to find solutions, such as setting up viable debt repayment plans, rather than ignoring the problem and continuing to chase for debt.

understanding of credit files

In its recent market investigation, the Competition and Markets Authority raised issues about consumers' misunderstanding of different types of credit search and what impact they have on consumers' credit files and credit scores. The CMA is consulting on possible ways to address the problem.[86]

We saw a strong echo of this lack of clarity in our own review. One of the biggest themes emerging from the complaints we examined was consumers' lack of understanding about how credit files and credit reference agency information work in practice. It is a complex area and presents challenges well beyond payday lending. It is possible individual businesses could do more to avoid some complaints by being clearer with consumers on their approach, for example by giving greater notice ahead of a registering default. But generally it is clear that more could be done to improve public understanding of how credit systems operate, particularly among vulnerable groups and those who have had problems with credit.

what can businesses do?

- **Work with credit reference agencies to ensure that consumers' credit files are accessible, transparent and easy to understand.** More needs to be done by industry and the credit reference agencies to improve clarity and build consumers' understanding in this area. It is particularly important for those who have experienced impaired credit in the past.

> "The ombudsman service industry seminar was well structured and useful. It was good to liaise directly with adjudicators and ombudsmen."
>
> **payday lender**

> "There is a still a stigma attached to having debt problems. This can often be even more acute for those who have used payday lenders. Many consumers are embarrassed at the situation they are in."
>
> **Robert, adjudicator**

supporting consumers

As a service, we too often see consumers who end up in a situation they feel embarrassed about or are too ashamed to confront their debt issues early. It is important people don't feel trapped with nowhere to turn because of the stigma sometimes associated with payday loans. Consumers should not be afraid to ask for help and should speak up sooner rather than later before problems get out of hand.

consumers can make things better by:

- **Seeking debt help early.** It is easy for debts to spiral out of control quickly. Consumers who experience problems with their loan should make their lender aware as soon as possible. Lenders can freeze interest and charges and set up a reasonable repayment plan. Consumers can speak to their bank as well as creditors – the bank can cancel a CPA, for example.
- **Not being afraid or ashamed to complain.** The ombudsman service is here to help and can guide you through the process.
- **Getting free and independent debt advice.** Debt advice charities, such as StepChange, can help, or get in touch with the ombudsman. We can point you to people who can help you get on top of your debt problems for free. The Money Advice Service also has information and advice to help consumers get their finances back on track.

our own response

The work we have done to inform this insight report has also informed the approach of our own service. We already run an extensive consumer outreach programme and training events for consumer advisers across the UK, from Crawley to Conwy, Truro to Dundee. We are complementing that work with a new drive to raise consumers' awareness of the help we can offer to those experiencing problems with payday loans. We are experimenting with new ways in which we can offer that help in the handling of consumer enquiries and complaints. And we are working directly with payday lending businesses to improve their understanding of our approach and to help them better serve their customers.

Above all, we have a renewed determination to work in partnership with regulators, the industry, parliamentarians, debt charities and consumer bodies, to help bring together those best placed to tackle problems in the sector, to improve business practice and to help those consumers who find themselves in difficulty.

We will not hesitate to refer to the regulator businesses that continue to flout their obligations or who demonstrate unacceptable practice. This is our duty. But there is a clear need for collaborative action to broker solutions. As a service, the ombudsman intends to play a full and active part in that effort.

annex 1

about us

about us

The Financial Ombudsman Service can:

- look at consumer complaints which cannot be resolved by the business.
- award redress up to £150,000.
- make modest awards to complainants for trouble and upset.
- consider cases up to six years from the event the consumer is complaining about, or if later, three years from when the consumer knew, or could reasonably have known, they had cause for complaint.

background

The Financial Ombudsman Service was set up under the Financial Services and Markets Act in 2000 to resolve individual consumer complaints against financial businesses, such as banks, insurers, mortgage lenders, credit card providers and independent financial advisers.

The ombudsman service is independent and impartial and makes decisions on the merits of each case and on the basis of what is fair and reasonable.

The ombudsman deals with disputes about all kinds of money matters involving regulated financial services providers. It dealt with 512,167 complaints in the 2013/14 financial year.

The service is free to consumers. It is funded through a combination of a levy on the industry and case fees.

how we handle complaints

The ombudsman deals with complaints that have not been resolved by the business. Consumers must first direct their complaint to the business, giving it eight weeks to respond. If after eight weeks there has not been a satisfactory resolution the consumer can bring the case to the ombudsman. Cases must be brought to the ombudsman within six months of the business's final response letter.

An adjudicator will assess the complaint and give an opinion either to uphold or reject it. This decision can be appealed by either side – consumer or business. An ombudsman will then review the case and give a final decision, which is legally binding.

The Financial Ombudsman Service is not a regulator. It does not write rules for financial businesses or fine them if rules are broken. This is the role of the financial regulator, the Financial Conduct Authority (FCA).

how we work with the regulator

The Financial Ombudsman Service has a duty to inform the FCA if it has information which might be of assistance to it. We regularly send the FCA details about the number and types of complaints handled and also flag any serious concerns we have about a firm's complaint-handling or the fitness and propriety of a firm or approved person, and any other issues that may require regulatory action. We also regularly answer specific requests from the FCA when they are investigating particular issues or businesses.

references

chapter 1

1 Source: Competition and Markets Authority, *Payday lending market investigation. Provisional findings report*, June 2014, p. 12.

2 Ibid., paragraph 14, p. 12.

3 Financial Conduct Authority, *Proposals for a price cap on high-cost short-term credit*, Consultation Paper CP14/10, July 2014, paragraph 3.8, p. 16.

4 Total UK consumer credit (excluding mortgage lending and student loans) stood at £160.6 billion in May 2014. Source: Bank of England, *Money and Credit: May 2014,* Statistical Release, 30 June 2014. Research by the Centre for Social Justice using Bank of England data showed that total UK household debt (excluding mortgages) rose from £5,495 per household in 2001 to £6,007 in 2012. See: Centre for Social Justice, *Maxed Out: Serious personal debt in Britain*, November 2013, p. 33. A Populus poll of 6,300 people for Which?, conducted between December 2013 and February 2014, found that one in six families were covering essential costs with payday loans or unauthorised overdrafts, or were defaulting on household bills. Two in five people (40%) were worried about household debt. See: "1 in 6 families struggling to pay bills in poorest areas", *The Guardian*, 17 July 2014.

5 The Poverty and Social Exclusion research project, funded by the Economic and Social Research Council, found that more than 30 million people – almost half the population – are now suffering to some degree from financial insecurity. The project, the largest study of poverty ever conducted in the UK, found that around a third of people suffer significant financial difficulties and about one quarter has an unacceptably low standard of living. See PSE UK/Economic and Social Research Council, *The Impoverishment of the UK. PSE UK first results: Living Standards*, March 2013.

6 Source: Financial Conduct Authority, *Proposals for a price cap on high-cost short-term credit*, Consultation Paper CP14/10, July 2014, paragraph 3.12, p. 17. Clearly, not all payday loan customers will be experiencing difficult financial situations, or will subsequently experience problems with their loan. A study undertaken by the former Competition Commission found that three in ten payday lending customers had an annual household income of £36,000 or more, and that 63% of customers repaid their loans on time and did not require another to get by. See: Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014, p. 12 and p. 116.

7 Payday lenders may allow borrowers to defer or extend their loan for another month by paying the interest owed on the due date. The lender will typically add a rollover or refinancing charge.

8 A CPA represents the consent given by a consumer for a business (e.g. a payday lender) to make requests to the consumer's payment service provider (e.g. their bank) for automated payments. Once consent is given, the business does not need to seek permission each time it requests a payment. The day and amount of money taken via a CPA can vary each time.

9 Financial Conduct Authority, *Proposals for a price cap on high-cost short-term credit*, Consultation Paper CP14/10, July 2014, paragraph 1.8, pp. 6-7.

10 Ibid., Box 1, p. 61.

11 Financial Conduct Authority, *Proposals for a price cap on high-cost short-term credit*, Consultation Paper CP14/10, July 2014, Box 1, p. 61. The Consumer Finance Association has been quoted as expecting the sector to shrink by about half in the coming years. See: "Watchdog set to unveil details of cap on UK payday loan charges", *Financial Times*, 13 July 2014.

chapter 2

12 The ombudsman service handled 2,357,374 initial enquiries and complaints from consumers in 2013/14, almost 8,000 each working day. Of these enquiries, 512,167 turned into a formal dispute, with 78% of new cases being about the sale of payment protection insurance (PPI). Source: Financial Ombudsman Service, *Annual Review 2013/14*, May 2014, p. 1.

13 Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014, p. 16.

14 Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014, p. 22.

15 Complaints against WDFC UK Ltd constituted just under 30% of the total number of new complaints about payday loans brought to the ombudsman by consumers in 2013/14. This seems to be in line with Wonga's overall market share: the Competition and Markets Authority state that Wonga has a 30-40% share of all loans by volume, and a 20-30% share of total payday revenue. See Competition and Markets Authority, *Payday lending market investigation. Provisional findings report*, June 2014, paragraph 2.77, p. 2-26.

16 Source: Financial Ombudsman Service, *Annual Review 2013/14*, May 2014, p. 83.

chapter 3

17 Competition Commission, *Payday Lending Market Investigation. Statement of issues*, August 2013, paragraph 10, p. 2.

18 Financial Conduct Authority, *Detailed rules for the FCA regime for consumer credit*, Policy Statement PS14/3, February 2014, p. 45.

19 The similarity between the respective profiles is not surprising given that the sample of cases analysed comprises such a signification proportion of the payday loan complaints considered by the ombudsman service in the last financial year.

20 The vast majority (97%) of complaints brought to the ombudsman service on consumers' behalf by claims-management companies in 2013/14 were complaints about payment protection insurance (PPI). The ombudsman service emphasises to consumers that they don't need the help of a claims-management company to bring a complaint. We look at the facts, not at how "professionally" a case is presented to us – and we prefer to hear from people in their own words. We do everything we can to make our service as straightforward as possible to use. So while consumers may choose to have someone represent them, we do things in a way that makes sure it is not necessary. We found no evidence that complaints brought to us by a claims manager in the last financial year were any more likely to be upheld. See: Financial Ombudsman Service, *Annual Review 2013/14*, May 2014, p. 39.

21 See "Ombudsman urges people to confront their fears and speak up about payday loan debt", Financial Ombudsman Service media release, 8 July 2014.

22 This trend was also clearly visible in the consumer survey undertaken as part of the former Competition Commission's payday market investigation, where 79% of payday customers had taken out more than one loan, with 66% having taken out three or more loans. Interestingly, although most customers had taken out more than one loan, the majority (55%) of customers had only ever taken out a loan through one lender. See: Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014, pp. 32-33.

23 See: Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014, p. 37. Data on the size of loan comes from transactional data supplied by payday lenders.

24 Loans extending beyond 31 days could be evidence of rollovers or similar loan extensions, or in some cases a sign of defaults and repayment problems. Financial hardship and vulnerability are explored further in chapter 10.

25 Clearly, this will not accurately reflect how the wider payday loan market operates. A study undertaken by the former Competition Commission, for example, found that 63% of customers repaid their payday loans on time and did not require another loan in order to get by. See: Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014, p. 116.

chapter 4

26 Care should be taken in the reading of results relating to cases featuring allegations or suspicions of fraud in this analysis. In most of these cases, the allegation of fraud was the dominant feature of the complaint, and it was less common for there to be subsidiary or additional features to these complaints. This runs counter to the trend visible in the remaining cases sampled, where complaints were frequently found to blend a mix of factors. This is discussed in greater depth in the next section. And as the tables make clear, it was very rare for an allegation of fraud to be a subsidiary feature of other complaints: where it did feature, it was predominantly as the main reason driving a complaint.

chapter 5

27 Office of Fair Trading, *Payday Lending Compliance Review. Final Report*, March 2013, p. 27.

28 CIFAS, *Fraudscape. Depicting the UK's fraud landscape*, 2014 Edition, p. 39.

29 Office of Fair Trading, *Payday Lending Compliance Review. Final Report*, March 2013, p. 27. In August 2012 the OFT revoked the licence of online payday lender MCO Capital Ltd and imposed a fine of £544,505 for failure to perform adequate identity checks on loan applicants.

30 See: "3 in 4 payday loans could have cause for complaint to the Ombudsman", Citizens Advice press release, 5 August 2013.

chapter 6

31 Competition and Markets Authority, *Payday lending market investigation. Provisional findings report*, June 2014, paragraph 5.21, p. 5-7.

32 Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014, p. 29. In a survey of 2,000 customers of high-cost short-term credit commissioned by the FCA, 24% said they chose to apply for HCSTC because it was their only option. The FCA's research also found that 64% of HCSTC customers had outstanding debt from other types of lender, that 55% said they used loans for everyday expenditure (such as housing, basic living costs and bills), and that 65% had no savings – compared to 32% of the UK population. Source: Financial Conduct Authority, *Proposals for a price cap on high-cost short-term credit*, Consultation Paper CP14/10, July 2014, paragraph 3.13, p. 17.

33 *Principles for the Reporting of Arrears, Arrangements and Defaults at Credit Reference Agencies*, January 2014, p. 6.

34 See: "Unlocking your credit report", Which? press release, 17 May 2014.

35 In July 2012 GE Money said that it would not approve mortgages for consumers who had taken out a payday loan in the past three months, or had had two or more payday loans in the past year, saying that it viewed this form of borrowing as 'indicative of financial stress' (see: "GE Money refuses mortgages to payday loan borrowers", *The Guardian*, 12 July 2012). A November 2013 survey of mortgage brokers by *Mortgage Strategy* magazine, on behalf of the BBC's *Newsnight* programme, found that two-thirds of brokers (64%) had had a borrower turned down for a mortgage because the borrower had previously had a payday loan (see: "Principality stops lending to payday loan users", *MoneyMarketing*, 17 February 2014). The same article reported that, in February 2014, Principality Building Society announced that it would no longer accept consumers for a mortgage if they had had a payday loan in the past 12 months – even if it had been fully repaid on time.

36 Such a theory is supported in part by evidence given by Lloyds Banking Group to the Competition and Markets Authority in its recent market investigation. The bank stated that it monitored the proportion of lending to customers with payday loans as these customers tended to have worse repayment behaviour than customers who did not use payday loans, representing a higher credit risk. Another large bank told the CMA that consumers with recent payday loan borrowing had default rates up to ten times higher than those customers without payday loans. See Competition and Markets Authority, *Payday lending market investigation. Provisional findings report*, June 2014, paragraph 5.31, p. 5-9.

chapter 7

37 "Consumer credit countdown – Review into debt collection practices of payday lenders starts on day one of FCA regulation", FCA press release, 12 March 2014.

38 Ibid.

chapter 8

39 It is conceivable that even this higher figure could understate the degree of consumer unhappiness with the use of CPAs, as consumers may complain directly to their bank about their operation.

40 Consumer Finance Association (CFA), Consumer Credit Trade Association (CCTA), BCCA, and Finance & Leasing Association, *Good Practice Customer Charter. Payday and Short-term Loans*.

41 Source: FCA, *Detailed rules for the FCA regime for consumer credit*, Policy Statement PS14/3, February 2014. See also "Tougher rules for payday lenders take effect", FCA website, 1 July 2014.

42 "Continuous payment authorities: it is your right to cancel", FCA website, 28 June 2013, available at: www.fca.org.uk/news/continuous-payment-authorities.

43 Source: UK Payments Administration Ltd.

44 Office of Fair Trading, *Payday Lending Compliance Review*, March 2013, p. 22.

45 "Citizens Advice calls for 'health warnings' in payday loan marketing", Citizens Advice news release, 11 September 2013.

46 FCA, *Consumer Credit Research: Payday Loans, Logbook Loans and Debt Management Services*, April 2014, p. 20.

chapter 9

47 Citizens Advice, *Holding payday lenders to account: half year results from the Citizens Advice payday lending survey*, July 2013, p. 2.

48 Department for Business, Innovation and Skills, and TNS BMRB/University of Bristol, *The impact on businesses and consumers of a cap on the total cost of credit*, March 2013, pp. 28-29.

49 Office of Fair Trading, *Payday Lending Compliance Review. Final Report*, March 2013, p. 2.

50 Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014, p. 113.

51 Competition and Markets Authority, *Payday lending market investigation. Provisional findings report*, June 2014, p. 6-31.

52 Financial Conduct Authority, *Proposals for a price cap on high-cost short-term credit*, Consultation Paper CP14/10, July 2014, paragraph 1.8, pp. 6-7.

53 We look more closely at the experiences of vulnerable consumers in chapter 10.

54 Clearly, we must allow for an inevitable margin of error in such a comparison. Consumers are not obliged to tell the ombudsman service about their personal circumstances, and for the purposes of our review we simply recorded instances where evidence of a consumer's potential vulnerability – from financial hardship to unemployment – was *visible* in the case file. It is both possible and likely that further consumers in our sample might have been experiencing financial hardship, but that it simply wasn't observable in the file. The proportion of consumers considered 'vulnerable' for the purposes of our review might therefore be an underestimate.

55 "StepChange Debt Charity welcomes payday loan announcement", StepChange press release, 13 May 2014.

chapter 10

56 Competition Commission/TNS BMRB, *Research into the payday lending market. Report*, January 2014, p. 12.

57 Ibid., p. 29.

58 Competition and Markets Authority, *Payday lending market investigation. Provisional findings report*, June 2014, paragraph 5.21, p. 5-7. The CMA found that some payday loan customers *did* have credit alternatives available to them: 18% of the customers they surveyed said that they could have used a credit card to borrow the money instead of a payday loan; 20% said that they could have used an overdraft; and 30% said that they could have used at least one of these two alternatives.

59 When a borrower is unable to meet their contractual debt repayments, they may complete an income and expenditure assessment and offer to pay a reduced – and affordable – amount back each month instead. This is known as a debt repayment plan. Usually, interest and charges are frozen so that the consumer can repay their outstanding balance, albeit over a longer term.

60 The Tax Incentivised Savings Association has found that 30% of UK households have no savings at all and that a further 20% have less than £1,500 to help them cope with an unexpected event or loss of income. See: TISA, *The Savings and Investments Policy Project: Our Financial Future. Review summary*, April 2014, p. 3. Statistics compiled by consumer group Which? suggest this is an even bigger problem among payday loan borrowers, where 55% have no savings. See: Which?, *Credit Britain: Making lending work for consumers*, May 2013, p. 8.

61 Competition Commission, *Payday Lending Market Investigation. Payday lender pricing working paper*, February 2014, p. 12.

62 Research by the University of Bristol found that as many as 40% of online borrowers and up to 60% of high street borrowers said that payday loans had trapped them into a cycle of borrowing. See: Department for Business, Innovation and Skills, and TNS BMRM/University of Bristol, *The impact on businesses and consumers of a cap on the total cost of credit,* March 2013.

63 Office of Fair Trading, *Payday Lending Compliance Review*, March 2013, pp. 14-15.

64 By way of comparison, in the sample of cases with no evidence of vulnerability or hardship, 21% demonstrated good practice and in 17% of cases there was evidence of bad practice. The remaining cases had no evidence either way.

65 See, for example, Which?, *Credit Britain: Making lending work for consumers*, May 2013; and Citizens Advice, *Holding payday lenders to account*, July 2013, p. 4.

66 "Debt advisors told us that lenders tended to focus on recovering the debt rather than on negotiating an alternative repayment plan, freezing or reducing interest and charges or suspending collection activity." Source: Office of Fair Trading, *Payday Lending Compliance Review*, March 2013, p. 22.

67 Office of Fair Trading, *Payday Lending Compliance Review*, March 2013, p. 15.

68 "Dealing with debt stress", StepChange website: www.stepchange.org/Howwecanhelpyou/Debtadvice/Dealingwithdebtstress.aspx.

69 "The Relationship between personal debt and mental health: a systematic review", *Mental Health Review Journal*, Vol. 15, Iss 4. See also: Royal College of Psychiatrists/Rethink, *Debt and mental health. What do we know, what should we do?*, 2011, Abstract, p. 3.

chapter 11

70 A review of 38 complaints conducted in August 2013 found that 50% had no final response letter on file. Four cases out of the 38 had a final response letter but it did not include referral rights. This research has been used by the ombudsman service's payday loans team to work with businesses to improve the quality of final response letters and the effective provision of referral rights.

71 To support this point, our analysis found some evidence to suggest that more established firms (as determined by the date of their OFT licence) had a better record on referral rights than newer lenders.

72 The ombudsman service gives all businesses four weeks from the date of the decision to pay redress and follow through on all other aspects of the decision, such as amending a consumer's credit file.

chapter 12

73 Mike O'Connor, StepChange chief executive, has commented: "On issues such as affordability checking, rollover and repeat borrowing, there is an urgent need for more radical reform". See "Payday loan problems up 82 percent", StepChange press release, 27 February 2014.

74 Department for Business, Innovation and Skills, and TNS BMRM/University of Bristol, *The impact on businesses and consumers of a cap on the total cost of credit,* P45, March 2013.

75 "CFA supports Callcredit's real time reporting solution", CFA press release, 25 June 2014.

76 Competition and Markets Authority, *Payday lending market investigation. Provisional findings report*, June 2014, Chapter 2, p. 26.

77 "Wonga looks beyond payday to try out longer loans", *The Guardian* 26 March 2014.

78 Competition and Markets Authority, *Payday lending market investigation. Provisional findings report*, June 2014, p. 4-60.

79 Ibid., p. 209.

80 Department for Business, Innovation and Skills, and TNS BMRB/University of Bristol, *The impact on businesses and consumers of a cap on the total cost of credit*, March 2013, p. v.

81 Source: Competition and Markets Authority, *Payday lending market investigation. Provisional findings report*, June 2014, p. 6-35.

82 6 April to 21 July 2014.

chapter 13

83 See, for example, Financial Ombudsman Service, *ombudsman news*, Issue 109, April/May 2013.

84 Consumers are also central to the FCA's approach to supervision of markets. When the new regulator came into force in April 2013 it was given a mandate by Government to put consumers at the heart of what it does and to ensure consumers are given a fair deal.

85 There are some positive early signs of this. For example, the new chairman of Wonga, Andy Haste, has commented: "We will become a more customer focused, and inevitably in the near term, a smaller less profitable business. However, we are determined to make the necessary changes and serve our customers in the right way, to repair our reputation and become a business with a long-term future and an accepted place in the financial services industry." See: "Wonga chair predicts drop in profits ahead of business review", *Money Marketing*, 14 July 2014.

86 Competition and Markets Authority, *Market Investigation into payday lending: Notice of possible remedies under rule 11 of CMA Rules of Procedure*, 11 June 2014, p. 12.

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