A total cost cap on the rent-to-own market

A response to the FCA's consultation on a cost cap on the rent-to-own market

Executive summary

The Financial Conduct Authority's (FCA) decision to consult on a cap on the cost of rent-to-own goods is a positive step towards addressing the problems associated with this market.

In 2017, Citizens Advice helped 5,127 people with rent-to-own debts. These rent-to-own consumers tended to be heavily indebted or showed signs of being vulnerable. They are often single parents, almost never have a mortgage or own their home, and a large number are out of work due to poor health. Commonly, they hold more than £8,000 of debt.

Rent-to-own products are useful for consumers - they allow people on low incomes to purchase goods that they cannot afford to pay for upfront. Clients who use rent-to-own stores value the convenience and feel that there are a lack of alternatives.

However, action is necessary to prevent people paying over the odds for rent-to-own goods. At present, rent-to-own goods are excessively expensive. Interest rates can be as high as 99.9%, and missed payments are subject to fees of £10-12 per occasion. More generally, rent-to-own goods are a bad deal - with high markups on prices, costly delivery charges, and expensive add ons, such as aftercare and insurance.

A total cost cap would be the most effective way to prevent these costs spiralling. A total cost cap would limit the damage that rent-to-own goods can do to people's financial situation in two ways. A limit on the total cost cap would:

- **Make rent-to-own products more affordable** - by limiting the upfront cost of the good, installation and delivery fees, and the level of interest charged, a total cost cap would reduce the outstanding levels of debt held by rent-to-own clients.
- **Reduce the cost of late payment fees** - nearly 60% of rent-to-own clients are charged late payment fees. These charges commonly amount to £72 over the course of a loan.

Competition and information remedies are unlikely to work. Rent-to-own customers tend to urgently need the good they purchase. This sense of necessity means these customers are unlikely to shop around or compare prices - circumstances which would limit the effectiveness of information or competition based solutions. The likelihood that such measures would work is further reduced by the high levels of vulnerability common to customers, with nearly half (46%) experiencing a long term health condition or disability.

The cap on rent-to-own to own goods must be clear to consumers and robust to gaming. It should include a 100% total cost cap on the following components:

- A cap on the upfront price of the good - tied to RRP or a 'reasonable' price benchmarked to high street providers which sell the good upfront.
- Benchmarked delivery, installation and recycling costs.
- A £15 cap on default charges per agreement per year.

A cap on rent-to-own goods should be implemented as quickly as possible. The FCA has proposed that rules on the cap be 'in force' by April 2019. We think the FCA must meet this timeline in order to limit the massive harm caused by this high cost product.

1. What alternative solutions could there be to address harm from high prices?

The FCA's evidence and the experience of our clients expose the significant problems with the rent-to-own market - in which low income households find themselves paying 3 to 4 times the upfront cost when purchasing essential household items.

The FCA needs to introduce a cost cap in this market - to protect consumers from purchasing overpriced goods from the spiralling costs of rent-to-own credit. The urgent need for household goods and the high levels of vulnerability amongst rent-to-own consumers mean that information and competition remedies would be unlikely to be effective.

Finally, a total cost cap on rent-to-own products would provide clarity to consumers - ensuring that people never pay back more than twice what they borrow.

A. A cap on the total cost of rent-to-own goods would benefit consumers

The primary problem with rent-to-own goods is the excessive cost of the product. The FCA's analysis of the rent-to-own market supports Citizens Advice's conclusions that this market is exceptionally expensive. With consumers regularly paying nearly three times the original value of the good, and sometimes paying up to five or six times as much.

As the FCA has shown this cost is built out of a number of component parts:

1. A mark up on the upfront price of the good.
2. Expensive delivery and installation costs.
3. High interest rates.
4. Expensive add-ons.

A total cost cap on rent-to-own would help to limit the combined effects of the first 3 component costs (see Table 1), meaning that the ultimate price paid by consumers would be significantly less.

Table 1: Comparative cost of a rent-to-own good before and after a price cap

6kg washing machine	Price before cap[1]	Price after cap[2]
Upfront price of good	£265	£160[3]
Delivery and installation cost	£27	£45[4]

[1] These prices are based on averages between two major rent-to-own providers.
[2] This price is modelled on the structure of a cap that we have proposed in response to question 2.
[3] This is based on the price of a similar product from Argos sold in June 2018.
[4] Standard cost of delivery and installation found at comparable home appliance stores.

Total cost of credit	£293	£205
Additional cost in interest	£291	£205
Total cost	£584	**£410**
Savings		**£174 or 30%**

The savings associated with a cost cap would prevent consumers on extremely low incomes paying exorbitant prices. An analysis of our clients with rent-to-own goods shows that consumers on very low incomes, and with other indicators of financial vulnerability, are more likely to struggle with rent-to-own debts.

Figure 1: Demographics of rent-to-own debt clients compared with debt clients and the UK population as a whole

Rent-to-own consumers tend to be heavily indebted. The FCA's prior research found that consumers with rent-to-own goods tended to have a number of debts - with an average debt to income ratio which rose from 14% in 2015 to 29% in 2016. Our data shows similar financial difficulties amongst our clients with rent-to-own debts - the median personal debt level amongst these clients is £8,193.

A total cost cap would limit the damage that rent-to-own goods can do to people's financial situation. Not only do people who have to take out rent-to-own goods tend to be in a financially vulnerable situation, but these products are often associated with a worsening of people's financial circumstances:

1. People who take out rent-to-own agreements tend to see their levels of total debt increase over the course of the agreement, whilst their income does not.[5]
2. People who take out rent-to-own agreements tend to see their credit history worsen, rather than improve.[6]

There are key ways in which a cap on rent-to-own products would reduce the level of financial harm caused by rent-to-own:

- **A total cost cap reduce the burden of late payment fees.** One of the elements which makes rent-to-own loans so unaffordable are late payment fees. Roughly 3 in 5 (58%) customers who purchase rent-to-own products miss payments and, amongst those who acknowledge missing a payment, the median number of missed payments is 6.[7] Missed payments tend to be charged at £12 per week, with a cap within a twelve month period. If these missed payments were distributed evenly across a 3 year loan, then consumers are likely to be paying an additional £72 over the course of their loan. Not only would a total cost cap reduce the burden of these fees, by reducing the weekly cost of the good it would also decrease the likelihood that customers miss payments.
- **A total cost cap would reduce people's level of outstanding personal debt.** The FCA's data also shows that rent-to-own goods tend to form a significant share of people's total personal debt levels. For people who took out a rent-to-own product between December 2015 and November 2016, the outstanding debts on these products amounted to between 34% and 38% of their total personal debt. A cap on the cost of rent-to-own credit would help reduce people's total level of debt and make the debt to income ratios of rent-to-own consumers more affordable.

In their analysis of payday loans the FCA found that 63% of consumers who were refused loans, believed they were better off without this form of credit. The high cost of rent-to-own products and the detrimental effects these goods tend to have on people's finances mean that - similarly - consumers are likely to benefit in the longer term from a cap on the cost of rent-to-own goods.

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[5] Amongst rent-to-own consumers who took out a loan in 2015, average personal debt has grown from £2000 per consumer to £4300. FCA, (2017) Feedback Statement: High Cost Credit, p.29

[6] People who took out a rent-to-own agreement in 2016 were likely to have fewer savings, and be missing payments more frequently one year into their rent-to-own agreement. FCA, (2017) Feedback Statement: Technical Annex, pp. 23-25

[7] Survey of Citizens Advice and Money Saving Expert clients, April 2018, sample 702.

B. Competition and information remedies alone are unlikely to work

The characteristics of the rent-to-own market mean that interventions which focus on increasing levels of competition and increasing consumer choice would be unlikely to produce better outcomes for consumers.

- **Rent-to-own goods tend to be essential household items, such as furniture or household appliances.**[8] As a result, consumers value convenience when it comes to purchasing household goods, as living without a cooker, washing machine or sofa is likely to significantly decrease quality of life, and increase daily living costs.[9] The importance of these items means that consumers are unlikely to extensively 'shop around' as most people are unwilling to 'go without' essential household items for more than a few days.
- **Financial circumstances reduce the choice available to consumers.** As we have seen, clients who purchase rent-to-own products tend to be on low incomes, have high levels of vulnerability and have a poor credit history. This radically reduces the choices available to consumers when shopping for essential utilities. Our research shows that nearly three-quarters of people who use rent-to-own shops do so because they couldn't afford to pay for a product up front. In addition, 1 in 3 rent-to-own consumers have been turned down for retail credit elsewhere.
- **A significant proportion of rent-to-own consumers are vulnerable and find it difficult to shop around.** Nearly half of our clients with rent-to-own difficulties experience a long term health condition or disability. For these clients, shopping online, comparing between providers, or accessing alternate suppliers of household goods (such as charities or the local authority) may be arduous. In addition, these vulnerabilities combined with a low income might leave people responding to the effects of a 'scarcity mindset': a tendency for those who are worried about their financial situation to have less cognitive capacity to devote to other areas of their life.[10]

There's also a lack of competition between retailers.

- **There are only two major high street providers of hire purchase goods.** One of these providers, PerfectHome, operates largely in the North-West of England. The concentrated nature of this market means that there is likely to be little pressure on prices, and leaves vulnerable consumers paying over the odds for rent-to-own goods.
- **Alternatives struggle to compete with the convenience and ease of high cost rent-to-own providers.** A number of initiatives are seeking to establish themselves as alternate low or mid-cost credit providers for those purchasing household goods. These initiatives are welcome and can provide much better

[8] In a survey of people who had used rent-to-own products in August 2016, 72% of the goods that respondents stated that they had purchased were household goods, such as an item of furniture or a household appliance. If we include a TV as an essential household appliance, this proportion increases to 90%.
[9] Through laundrette services or pre-prepared meals for example.
[10] Mullainathan, S. Shafir, Scarcity: The true cost of not having enough. 2014.

value for consumers. Unfortunately, these initiatives tend to operate on a relatively small scale and are often little known about - meaning that they struggle to compete at scale against high cost rent-to-own providers.[11]

C. The total cost cap will provide clarity to consumers

A lack of clarity over the eventual cost of rent-to-own goods has been a recurrent theme in the FCA's analysis. In our 2016 survey, more a quarter of people who purchased a rent-to-own good were not sure what the total amount they had to pay was.[12]

Increasing price transparency has not significantly reduced the detrimental effects of these goods. The FCA's work with rent-to-own providers has made steps towards increasing the clarity of pricing structures, especially when it comes to goods sold online. These changes have not had a transformative effect on the way people purchase rent-to-own goods, and we continue to see customers paying 3 times the off the shelf cost of the good. Evidence from our advisers and the FCA suggest that this might be due to a strong emphasis on the weekly price of the good when items are purchased in store.[13] This is exacerbated by consumer tendencies towards overconfidence, with a significant number of rent-to-own users overestimating their ability to meet the cost of the hire purchase arrangement over three years.[14]

Some consumers struggle to understand the cost of rent-to-own goods. In addition to a lack of choice when purchasing household goods,some clients - due to a mental health difficulties, a shortage of time or a lack of financial capability - do not clearly understand the cost of the rent-to-own good at the time of purchase.

Case study: Eileen

Eileen is a 74 yr old widow living in private rented housing. Eileen is blind in one eye and has struggled with a learning difficulty throughout her life. She currently has no savings, and debts of nearly £6,000. At the moment, Eileen owes a rent-to-own provider £550 for a tablet computer, a mobile phone and a vacuum cleaner. She struggles to meet her weekly payments of £75.60 to the store, but despite her inability to pay, Eileen finds herself persistently being contacted by the store to purchase 'new and better' goods.

Our advisor recounts that Eileen; *'Has enough to live on, but struggles to understand the high interest rates charged on the goods... [When she is contacted], she feels vulnerable and finds it hard to say no.'*

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[11] Financial Inclusion Centre, (2016) *Better and Brighter: Responsible Alternatives to the rent-to-own Sector*.

[12] PWC's report into rent-to-own users also suggested that many consumers did not anticipate the total cost of their rent-to-own good, especially when it included extras. PWC, Usage and Experiences of High Cost Credit, April 2018, p.30-32.

[13] FCA, High Cost Credit Review, May 2018, p. 21.

[14] PWC, Usage and Experiences of High Cost Credit, April 2018, p.30-32.

A total cost cap is the most effective way of preventing consumers from paying over the odds for rent-to-own goods. In analysis we conducted with payday loan users after the cap, 81% told us that - at the outset - it was clear what they would owe.[15] This clarity in the maximum sum that can be charged for rent-to-own good will allow consumers to better budget and assess the affordability of a good, as well as allowing consumers to price compare with other similar products.

[15] Citizens Advice, Payday loans after the cap: are consumers getting a better deal?, August 2016

2. What issues should we take into account in carrying out further work on a price-cap?

A. The structure of a cap on the rent-to-own market

i. A cap on manufacturer's retail price

We propose that the rent-to-own cap would take the form of a 100% total cost cap. A cap on the cost of credit would use the permissions introduced under section 137C of the Financial Services and Markets Act, as amended by the Financial Services (Banking Reform) Act 2013. The Act gives the FCA a power to put a limit on the cost of credit. The FCA should use that power to protect rent-to-own consumers from excessive costs and charges.

A total cost cap should be linked to the recommended retail price of a product or a 'reasonable' benchmarked price. Electronic goods and household appliances supplied by manufacturers in the UK and abroad have a recommended retail price (RRP). [16] Within a rent-to-own credit agreement, the recommended retail price would be equivalent to the current 'product price' or the 'price/amount of credit'. The total cost cap would limit the cost of a good to be 100% of the total recommended retail price.

The Australian model of capping rent-to-own goods
The Small Amounts Consumer Credit (SACC) Review made a number of recommendations to address these issues, including:

- Capping fees at 4% of the Base Price of the goods per month, for a maximum of 48 months.
- Capping consumer lease repayments to 10% of the consumer's net income.
- Banning unsolicited selling of consumer leases.[17]

This approach echoes the approach of the Australian government's Small Amounts Consumer Credit (SACC) review (see box). The SACC proposal however, applies to consumer leases - this means that consumers do not necessarily end up owning the good at the end of the purchase arrangement. As a result, the 4% fee cap as a proportion of base price would be very low within a hire purchase term - and prevent consumers purchasing rent-to-own goods on a 1 year purchase term.

Goods sold by rent-to-own shops without a RRP - due to their bespoke production - should be benchmarked with other similar products. A significant proportion of rent-to-own goods are furniture, which tends to be built in house. There are however, comparable products available which have comparable features. It is important that these goods are benchmarked, as they often show the biggest markups on price - leaving customers regularly paying up to 4 times the cost of a comparable product before including the costs of add-ons and insurance.

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[16] Recommended retail prices were banned on electronic goods in 1998 - due to fears that they were increasing prices, but increasing levels of competition in electronic goods markets have seen them reintroduced by the Competition Commission in 2012.
[17] The Financial and Consumer Rights Council, The SACC Review, March 2017

Second hand goods sold at 10% less per six months of prior use since manufacture or benchmarked to household products of similar characteristics and age. Most household appliances cease to be considered valuable after a 5 year period.[18] With the life expectancy of a significant number of products sold by rent-to-own providers to be between 5-10 years.[19] We propose that every 6 months of use should decrease the RRP by 10%, with consequent effects on the total cost cap.

What are the benefits of a total cost cap tied to RRP?

A limit on the total cost of credit tied to a recommended retail price would prevent rent-to-own firms artificially inflating the upfront price of the good. This practice is already widespread amongst rent-to-own providers.[20] A simple cap on the cost of credit would risk making this practice more common.[21]

A total cost cap - linked to an RRP - would provide clarity to consumers. Our research has shown that a significant proportion of consumers do not clearly understand the total cost of hire purchase goods when they take out the agreement. A total cost cap would ensure that consumers are clear about the total cost of the product that they are purchasing.

A total cost cap would be straightforward to assess through supervision. The FCA has undertaken extensive supervision of the rent-to-own sector, including redress schemes of £17 million for consumers. A total cost cap would make it easier for the FCA's supervisory function to identify excessive costs for consumers or where consumers might be overcharged.

ii. A cap should ensure no consumer spends more than 20% of their income on rent-to-own agreements.

Affordability remains a major problem with rent-to-own goods. In our 2016 survey, we found that 1 in 5 rent-to-own customers were paying more than 20% of their income on rent-to-own goods.[22]

Affordability checks need to take place on every occasion that a rent-to-own good is purchased. In our 2018 survey of Money Saving Expert clients who took out rent-to-own goods, a third of respondents said they were not asked 'about [their] personal finances and general situation to see if [they] were able to pay for the products'. And amongst those who did experience affordability, less than half (45%) had affordability checks every time they took out a loan.[23]

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[18] http://www.ukwhitegoods.co.uk/help/buying-advice/consumer-help/3669-what-your-appliance-is-worth

[19] These estimates are US based, but the same considerations seem likely to apply in the UK. Appliance lifetimes, Consumer Reports 2009 and Life Spans of Home Appliances, NAHB

[20] Citizens Advice, Rent to Return, March 2018 and FCA, High Cost Credit Review, May 2018

[21] The FCA highlighted this risk in their High Cost Credit Review, July 2017

[22] Citizens Advice, Hire purchase: Higher prices. Problem debt in the rent to own market, November 2016, p15.

[23] Survey of 702 Money Saving Expert Readers with 200 rent-to-own customers, April 2018.

In keeping with the approach of the payday loan cap and the SACC, there should be a package of measures to protect consumers in the rent-to-own market. A cap on spending as a proportion of income would protect very low income consumers from taking out loans which they are likely to struggle to afford, as well as limit the detrimental effects of multiple rent-to-own products on people's finances.

To ensure no customer pays more than 20% of their net income rent-to-own repayments, an affordability check must be undertaken every time a customer takes out a rent-to-own item. The FCA should then supervise this measure to ensure that - at the outset of an agreement - no customer is committing to paying more than 20% of their net income towards the cost of rent-to-own goods.

iii. Installation, recycling and delivery should be benchmarked, and included within a total cost cap

Currently, rent-to-own goods have disproportionately expensive installation and delivery costs. The average price of installation and delivery at one of the major rent-to-own providers is 61% higher than comparable costs at other high street stores.[24] These installation and delivery fees - after being subject to interest - represent nearly two fifths of the total cost of the rent-to-own item.[25]

Installation, recycling and delivery costs should be to benchmarked against other high street household goods suppliers. This would limit the extent to which rent-to-own providers could overcharge consumers for those services.

Delivery and installation should be added to the upfront cost of the good. A total cost cap should be applied to the combined cost of the good and installation or delivery costs (if any). For a number of household appliances, high street competitors do not charge delivery costs, we would expect rent-to-own providers to match a reasonable benchmarked price.

An alternate solution to control installation costs could be introducing backend competition for installation and delivery. This would, however, be a complex process to introduce. It would also be likely to make rent-to-own products less convenient for customers - forcing them to go through an additional purchasing process.

iv. Late payment fees should be capped

Late payment fees are one component of the exorbitant cost of rent-to-own products. These charges tend to be between £10 and £12 per missed payment. Amongst customers we surveyed, the median number of late payment charges paid by those who miss payments is 6, amounting to roughly £70 across the course of the loan.[26]

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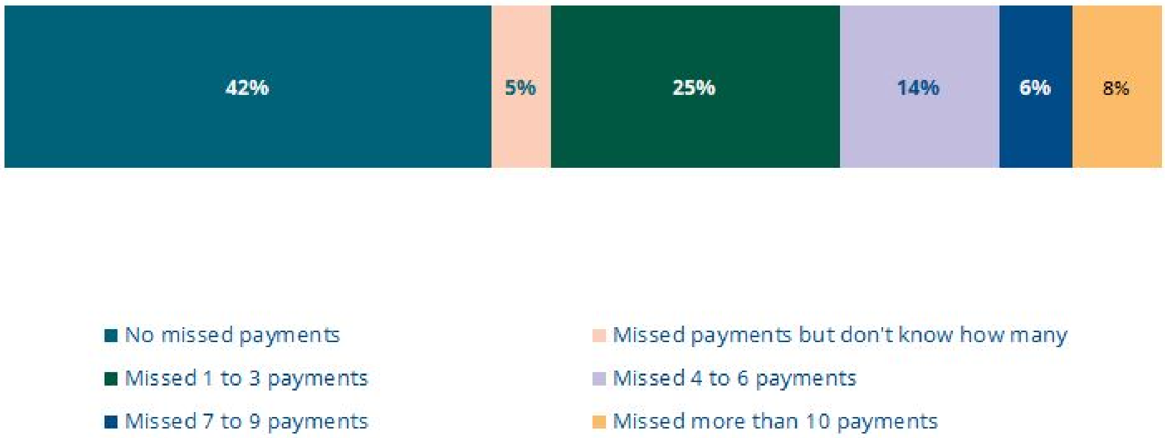
[24] The mean cost of installation and delivery across 4 household appliance products at Brighthouse was £67.50, 60% higher than at two comparable household appliance shops John Lewis and Argos where the mean cost of installation and delivery was £41.99.

[25] The mean cost of installation and delivery across household appliances was 37.1% of the total cost.

[26] Survey of 702 Money Saving Expert Readers with 200 rent-to-own customers, April 2018.

Figure 2. The number of late payment charges paid by those who had missed payments



As figure 2 shows, a large number of late payments charges are experienced by a small number of people. Just 8% of the rent-to-own clients we surveyed pay more than a third (36%) of the total missed payment fees of the entire group we surveyed. This could amount to nearly £190 of charges over a three year period - or an additional cost of 17% of the median original rent-to-own loan.[27]

Late payment fees should be capped at £15 per year of the loan agreement. The high cost short term credit cap placed a limit on default or late payment fees of £15 over the course of a loan. Introducing a similar cap on rent-to-own loans would bring the charges into line with the payday loan industry and provide clarity to consumers. It would also provide protection to 28% of rent-to-own consumers who miss four or more payments over the course of their hire purchase agreement.

The 100% total cost cap should represent the maximum that a customer could pay, *including late payment fees.* If interest on the good means that the hire purchase comes to double the price of the product RRP, then the additional default charges would not be added. This would ensure that the cost of an item remains clear to the consumer - and ensure that consumers can seek redress if they face excessive costs.

v. Extended warranties and theft and accidental damage insurance would not be included within the cap

We share the FCA's concern about the excessive cost of extended warranty products and theft and accidental damage guarantees purchased through rent-to-own stores. Our assessment of the structure of a cap suggests that it would be difficult to include these within the total cost cap. Instead, these add-ons should be sold on more restrictive terms. **All consumers should be given a 14 day cooling off period after purchase in order to shop around for aftercare and insurance.**

[27] The FCA's data found that the median Rent-to-Own loan origination was £1090. FCA, High Cost Credit Review, July 2017

Figure 3. The structure of a total cost cap

100% total cost cap of amount borrowed
(applying to all interest, fees and charges)
Amount borrowed = RRP or benchmarked price of product + benchmarked installation, delivery and recycling

£15 limit on default fees per item per year of the agreement	**20% cap** on payments as a proportion of consumer's net income

B. The impact of a cap on rent-to-own for consumers

A rent-to-own cap would bring much needed protection for consumers - primarily by reducing the total cost of often urgently required household goods. The example of the payday loan market - whilst involving a different cap structure - indicates that a cost cap on high cost credit products can be introduced with relatively few unintended consequences. In this section of our response, we set out what we imagine the wider repercussions of the total cost cap will be and how we think the FCA should address these issues.

i. A cap on the rent-to-own market is unlikely to significantly reduce access to credit

A total cost cap on rent-to-own goods would make these products significantly more affordable. By reducing the total cost of rent-to-own goods, it is likely that rent-to-own products will be available to more consumers rather than less. Our analysis of rent-to-own products across two rent-to-own providers suggests that a 100% total cost cap on the RRP of a good would reduce the costs to consumers by a median of 28% or £276.[28]

Table 2: Cost savings for consumers associated with a cap on rent-to-own goods

	6kg Washing Machine	50cm Electric Cooker	60cm fridge freezer	2 Seater Leather Sofa	32" HD Television
Average total cost between two major rent-to-own providers	£584.22	£666.90	£1,181.50	£1,754.22	£681.72
Cost of good at another store	£159.99	£256.99	£439.99	£549.99	£259.00
Installation and delivery costs[29]	£45.00	£14.99	£0.00	£6.95	£3.95
Cost with 100% total cost cap	£409.98	£543.96	£879.98	£1,113.88	£525.90
Savings	**£174 or 30%**	**£123 or 18%**	**£302 or 26%**	**£640 or 37%**	**£156 or 23%**

A limit on the costs of rent-to-own goods would decrease the likelihood of default. As we have shown, people who take out rent-to-own goods tend to be in a weak financial position which deteriorates over the course of their loan. At present, roughly half of rent-to-own agreements do not reach completion. A control on the costs would

[28] Based on price comparisons across 10 different rent-to-own products across the two major rent-to-own providers in June 2018, with a high street store purchased upfront.
[29] Benchmarked against installation and delivery costs for these products at comparison high street retailer.

reduce the riskiness of the loan and the likelihood that clients struggle to meet the costs of their agreement and default.

The major risk to access to credit of introducing a rent-to-own cap is the challenge to the rent-to-own provider business models. A total cap on rent-to-own goods would reduce the profitability of rent-to-own business models, although it would still allow them to charge significantly more than competitors. This might lead to a shrinkage in the size of the market for rent-to-own products - with consequent effects on access to this kind of credit.

iii. People who use rent-to-own goods are likely to have access to other sources of credit

People who use rent-to-own goods often have access to other of sources of credit. The FCA's credit reference data indicates that 52% of consumers using rent to own as of November 2016 also held home-collected credit debts, and 46% held catalogue credit debts.[30] Our clients with rent-to-own issues too, often have other consumer debts with 39% holding home credit debt and 32% with catalogue credit debt.

Home credit and catalogue credit would be more affordable than rent-to-own loans. The disparity between the costs of rent-to-own costs and home credit loans exposes the massive cost of rent-to-own loans in comparison with even other forms of high cost products. We would be wary however, of advocating that customers who purchase rent-to-own goods turn instead to home credit goods, as home credit loans encourage people to repeatedly refinance loans - with damaging effects on people's finances over the longer term.

It's unlikely that - if people were denied rent-to-own loans - they would turn to illegal lenders. Research by the Competition Commission in 2014 found that payday loans were commonly spent on everyday expenses, with 60% saying that they could not have gone without the loan.[31] In spite of this, the FCA's research after the cap found that the majority (63%) of people who were turned down for a payday loan felt they were better off as a result. In particular, the research did not identify an upsurge in illegal lending associated with payday loan rejection.

ii. Alternative providers would benefit from a more level playing field

The experience of our clients - and the data collected by the FCA - suggest that there are two key reasons behind the decision to purchase a rent-to-own product:

- A perceived lack of other options
- The immediacy and tangibility of rent-to-own options

These perceptions of rent-to-own provision are reflective of some of the shortcomings of alternate providers of low cost credit and emergency appliances - which are often small scale or not widely known. In part, responsible lenders struggle to develop the

[30] FCA, High-cost Credit Review: Consultation on rent-to-own, home-collected credit, catalogue credit and store cards, and alternatives to high-cost credit, May 2018, p.21.
[31] Competition Commission, Research into the payday lending market, 2014

increase the scale of their provision due to the difficulty of competing with the reach and convenience of profit making firms such as Brighthouse and Perfect Home.

Despite these limitations, alternatives resources for household items and furniture do exist. These take two forms:

1. **Credit unions and Community Development Finance Institutions (CDFIs) -** Credit unions and CDFIs can support people to access more affordable finance for household goods, and these schemes are seeking to scale up significantly.[32]

   We welcome the government's efforts to support financial inclusion - through the Financial Inclusion Policy Forum, as well as Department for Digital, Culture, Media & Sport's scheme for dormant bank accounts.

   To support these initiatives, the FCA should remove regulatory barriers to the sale of rent-to-own goods by credit unions. Credit unions are currently exempt from consumer credit lending regulation - meaning they are not able to sign the borrower-lender-supplier agreements necessary to directly supply household goods. To participate in these agreements, credit unions must secure authorisation to operate under a Consumer Credit Lending agreement or apply to FCA for Variation of Permission. These regulatory changes are both a cost to the credit union and can be time consuming - leading to additional regulation and reporting. This extra layer of bureaucracy can limit the attractiveness of schemes to provide household goods - such as that undertaken by Leeds Credit Union[33] - for smaller providers.

   But, not all people who are unable to purchase rent-to-own goods will benefit from commercially viable loans. Crucial to the success of government initiatives for financial inclusion is the recognition that some people will struggle to borrow at commercially viable rates. These consumers would benefit instead from no-interest loans or grants to meet the cost of household goods.

2. **Local welfare assistance and charitable schemes.** Local Welfare assistance schemes are operative in a significant majority of councils, with 85% of local authorities running a scheme in 2017/18. There are clear shortcomings in local welfare assistance schemes at present - they are difficult to access, are poorly publicised and can be restrictive in the support they provide. These schemes can however, support people to access household goods and appliances. In an interview with a Citizens Advice client who had used a local welfare assistance scheme in Derbyshire, we were told;

   > *"I got a washing machine, a fridge-freezer and it was pretty good… They got me to fill in a form about what I needed, I spoke to a council worker and I waited two weeks and then it came.'*

   In addition, there are a range of charitable schemes which operate locally through networks such as Reuse. As with local welfare assistance schemes,

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[32] http://responsiblefinance.org.uk/2017/11/we-need-a-bold-vision-for-the-provision-of-affordable-credit/

[33] https://www.leedscreditunion.co.uk/loans/homeware-loans/-

familiarity with affordable or charitable alternatives tends to be low. To respond to this, we would advocate that:

Providers should be mandated to provide information and signposting to alternate lending schemes and sources of local authority support, where consumers are declined for a rent-to-own loan.

iv. Despite these alternatives, there needs to be an expansion in the provision of mid and low cost credit

There has been a massive shrinkage in the availability of low cost credit. The last decade has seen a very significant contraction in the availability of low cost credit provided by government. The total value of budgeting loans has fallen by nearly a third since 2006/07. Crucially, this has been achieved by cutting the number of budgeting loans awarded by more than 350,000 in a one year period, in real terms the sum of money provided by budgeting loans by £170.

Figure 3. Government expenditure (in millions) on budgeting loans since 2006/07

The limited availability of government backed affordable credit leaves a gap in the market. This has often been filled by high cost credit providers. It has also brought people in a financially risky situation into the credit market when this might be inappropriate for their financial needs. The FCA's role in these circumstances is to ensure that those who are no longer able to access affordable credit do not experience excessive costs at the hands of high cost lenders.

To supplement these efforts, we propose that the FCA should do additional research to map the scale and causes of financial exclusion. At present, the figures on the number of people who are unable to access credit is 9 million.[34] Yet, this statistic is more than ten years old and uses unreliable proxies to estimate the proportion of people who are financially excluded.[35]

To understand the scale of financial exclusion as a social policy issue, the FCA should use credit referencing agency data to find out the number of people excluded from mainstream credit and the reasons behind this. This research would enable policymakers to develop more targeted responses to the issue of access to credit - ensuring that policymakers develop financial products which suit the financial circumstances in which people find themselves.

[34] New Economics Foundation, 2009. Doorstep Robbery: Why the UK needs a fair lending law, London: New Economics Foundation.
[35] The figure combines the 7.7 million people with a basic bank account and the 1.5 million who were unbanked in 2006.