Impact of consumer credit laws

In today's consumer based society, the need for credit is undoubted. More and more individuals and organisations are reliant upon credit to undertake their day to day activities, thus the role of credit in society has magnified in unmeasurable amounts. There are also more personal credit products available on the market than when the original *Consu me r Credit Act 1974* was drawn up, thus there is more of a need to regulate these products and the relationships between creditor and debtor in order to avoid any unfair conduct on the part of either party. As the Government White Paper suggests:

The laws governing this market were set out a generation ago. In 1971, there was only one credit card available; now there are 1, 300. 30 years ago, £32m was owed on credit cards; now it is over £49bn. The regulatory structure that was put in place then is not the same as the regulatory structure required today. As the credit market has developed, reforms have become necessary to modernise the current regime and update it for the 21st century. [1]

This evidence clearly supports the idea that the previous rules governing consumer credit relationships are significantly outmoded and outdated, and are in dire need of updating and reworking to meet the needs of a modern society. The nature of the relationship between a debtor and their creditor or supplier has subsequently become more complex and legalistic, and requires rules that govern these specific relationships without relying upon the general principles that can be found in, say, the *Unfair Terms in Consu me r Contracts Regulations 1999* , which will be discussed in more detail in due course. This brief intends to consider the new provisions of the *Consu me r*

Credit Act 2006 and determine whether this legislation goes too far in protecting the rights of debtors, as opposed to the rights of creditors and suppliers. These conclusions will be drawn based upon consideration of the primary legislation, including the previous *Consu me r Credit Act 1974* , as well as the apparent diverse and conflicting nature of secondary sources on this issue. It appears that a number of viewpoints could be explored, and this brief intends to do just that in order to arrive at the most appropriate conclusion. The Government had already completed a review of the 1974 Act in its White Paper, which will be discussed shortly. This Paper identified key areas where the law was not protecting the rights of consumers, and often allowed credit companies to take advantage of vulnerable individuals in order to rise to the top of what has effectively become a crowded and cut-throat marketplace. Each company is trying to sell its product to consumers, each trying to maximise the revenue it can make from it. In order to avoid innocent Britons from being exploited by unregulated corporations, the Government commission its review into the *Consu me r Credit Act 1974* before drafting the *Consu me r Credit Act 2006* , in order to ensure that the new law was going to address the most salient of concerns of consumers. It was also important to define who should be afforded protection under the new law. Should it be aimed at the general British consumer, or should it have specifications that restrict who could rely upon these provisions based upon certain socio-economic factors? This is where this report will begin.

Perhaps the best place to begin would be to continue considering the DTI's White Paper on consumer credit in the 21st century. While it does not consider the current *Consu me r Credit Act 2006* in express terms due to its publication several years before its enactment, it does highlight the perceived inadequacies of the then existing consumer credit protections of the *Consu me r Credit Act 1974* . Firstly, it appears that the Government is concerned with establishing a transparent marketplace that prevents debtors from being taken advantage of by creditors and suppliers. It plans to accomplish this by having clear and effective regulations in place to govern the use of advertising in selling credit products. [2] This intends to address the inadequacies provided not only by the 1974 Act, but also by the *Consu me r Credit (Advertise me nts) Regulations 1989* due to the recently explosive nature of consumer credit products and contracts. The rationale behind such a move by the government can only be suggested to attempt to protect the consumer against any deceptive or misleading conduct by creditors through advertising promotional campaigns that could unduly influence them into entering into consumer credit contracts which do not specifically cater for their needs or financial situations. This would be consistent with the notion that the intention of the 2006 Act is to protect the consumer/debtor more so than the creditor, due to their more vulnerable position in the marketplace. Quite obviously, disparity does exist between the negotiation and contractual powers of debtors and creditors, and thus the intention of the Government is to create a more level playing field, allowing them to do business in a manner which is not only legal, but also moral and ethical. Another way the Government claimed this will be done in its White Paper was through standardisation of the form of consumer credit contracts. [3] This would, theoretically, ensure that there are minimal differences between the standard terms of a consumer credit contract regardless of who the credit provider was, and regardless of what the actual lending product was. Again, this clearly is intended to protect the debtor more so than the creditor, given the disparity in contractual and negotiation abilities and resources available to the two parties. The Government even intends to reflect the changes in the way we contract that have come into existence since the 1974 Act, including online contracts. The rationale behind this is that the use of the internet in contractual dealings can often lead to an increased possibility of fraud on the part of either party. [4] What this means is that one could quite possibly enter into a contractual agreement through an online method without going through the full stringent identity criteria as they might be required to if they were personally entering into this agreement at, say, a bank. Normally a 100-point ID check, or similar procedure, may be used or relied upon by a creditor in order to ensure that they were dealing with the person whose name appears on the contractual documents. However, this may also extend to a debtor where the reliability of the credit provider could not be ascertained. This protection would then effectively protect both the creditor and debtor to ensure that the contract was reliable, and that the correct person or entity was included as a party to the agreement.

Perhaps the most important aspect of the Government White Paper regarding consumer credit contracts is the introduction of more stringent licensing criteria for credit providers. The Government's hope, in 2003, was that the reform to the consumer credit laws would give the Office of Fair Trading more power to investigate credit providers to ensure that they were complying with the terms of the license granted upon them. Previously, the DTI claimed that the tests that a credit provider was required to pass to gain a license only determined whether they initially met these criteria, and did not illustrate whether they continued to meet the criteria, and thus remain fit to provide credit to consumers. [5] This would, theoretically, maintain the integrity of the consumer credit industry, making it much safer for consumers to deal in the sometimes overwhelming credit market. Again, this appears to be protecting the consumer's interests more so than those of the credit supplier. The DTI has identified a number of areas that the *Consu me r Credit Act 1974* was lax in upholding and protecting in the interests of consumer credit, and it would appear that, based upon the general consensus of this White Paper (a fundamental research document that highlights the Government's intention in reforming particular laws) that the DTI is more concerned about consumers being taken advantage of due to developments in the credit market that tend to fall outside the scope of the 1974 Act. This is mainly due to social and technological advances that were not within comprehension at the time the 1974 Act came into enforcement and a lack of reform since that time. However, while the shortfalls of the Act have been duly illustrated by the DTI, what if a consumer continues to have a problem with a credit contract? To what institution do they turn to exercise their right of redress? The DTI uses its White Paper to harangue the idea of the Financial Ombudsman Service being empowered to investigate contractual dispute involving consumer credit. This would create an alternative dispute resolution pathway that may ultimately avoid the pomposity, risk and financial burden that was previously required in order to take a matter to court. Rather, this would make the dispute resolution procedure much more appealing and affordable to a consumer, giving them more opportunity to vindicate their legal rights where they might otherwise be precluded from doing so due to pressing financial commitments. This does gear itself towards the consumer more so than the creditor, as a credit providing company would presumably have a greater access to legal expertise and resources by comparison to the individual person, thus the DTI found it prudent to address the shortfalls of the 1974 Act in protecting individual debtors. While these have all been appropriately illustrated by the DTI's White Paper, it is important to note that this was simply and analysis of the 1974 Act in conjunction with today's developing credit-based society, and does not in itself give rise to any legal effect. It does, however, point out the reasons behind the Government's wish to reform consumer credit laws, and gives one a way to measure the effectiveness of the now enacted *Consu me r Credit Act 2006* by applying these criteria. It is now important to consider the express provisions of this Act in order to determine whether these shortfalls identified by the DTI have been adequately addressed and protected by the new Act.

Before considering the possible codification of the DTI's discussion in the *Consu me r Credit Act 2006* , it is important to establish the scope of application for this Act. It does not apply to businesses or corporations who enter into consumer credit contracts solely for business purposes. Rather, it serves to protect individuals that may be at less of a negotiation or contracting position than what a business would which may have access to virtually unlimited capital. The 2006 Act defines an ' individual' as:

(a) a partnership consisting of two or three persons not all of whom are bodies corporate; and

(b) an unincorporated body of persons which does not consist entirely of bodies corporate and is not a partnership. [6]

The inclusion of these two categories as ‘ individuals’ for the purposes of the Act gives more people protection under the Act than what may have been afforded otherwise under the 1974 Act, thus ensuring more consumers are protected. It clearly precludes large businesses and corporations from seeking protection under the Act, thus ensuring that only those who may not necessarily be able to provide their own legal protection are protected by law from being taken advantage of. Additionally, section 2 of the 2006 Act removes the previously existing financial limits for protection under the Act (£25, 000) [7] thus broadening the scope of application, however section 3 excludes consumers with a ‘ high net worth’ from also obtaining protection under the Act, which subsequently re-limits the scope of application to those consumers who really are in need of consumer protection. The presence of these provisions in the 2006 Act suggests that the intention of the Act is to provide protection for those that may otherwise be at a disability to do so of their own will and accord.

One of the most important changes that the 2006 Act has made to consumer credit regulation is the ability of a court to now hear matters relating to unfair credit relationships. The powers of the court in such circumstances have been defined, as have the procedural requirements for bringing such a matter before a court. [8] Under the newly amended sections of the 1974 Act, a court must have regard for the following factors when adjudicating on the issue of an unfair relationship:

(a) any of the terms of the agreement or of any related agreement;

(b) the way in which the creditor has exercised or enforced any of his rights under the agreement or any related agreement;

(c) any other thing done (or not done) by, or on behalf of, the creditor (either before or after the making of the agreement or any related agreement). [9]

Additionally, the remedies available to the court include:

(a) require the creditor, or any associate or former associate of his, to repay (in whole or in part) any sum paid by the debtor or by a surety by virtue of the agreement or any related agreement (whether paid to the creditor, the associate or the former associate or to any other person);

(b) require the creditor, or any associate or former associate of his, to do or not to do (or to cease doing) anything specified in the order in connection with the agreement or any related agreement;

(c) reduce or discharge any sum payable by the debtor or by a surety by virtue of the agreement or any related agreement;

(d) direct the return to a surety of any property provided by him for the purposes of a security;

(e) otherwise set aside (in whole or in part) any duty imposed on the debtor or on a surety by virtue of the agreement or any related agreement;

(f) alter the terms of the agreement or of any related agreement;

(g) direct accounts to be taken, or (in Scotland) an accounting to be made, between any persons. [10]

Essentially these provisions allow a debtor to challenge a consumer credit contract on the basis of it being ‘ unfair’ to them, and empower a court to take remedial action where the law was previously vague and uncertain. It affords the debtor further protection from a creditor, given them a clear indication of their rights where they believe they have fallen victim to unfair conduct. It may serve to exonerate them from a contract they were having difficulty to adhering to because the terms were quite clearly outside their ability to keep to, or similar arguments. While this does not fall under the jurisdiction of the Ombudsman, which will be discussed shortly, it still allows a debtor to seek protection from the law from a consumer credit contract that they must have otherwise been contractually obliged to perform. This does not suggest that avoidance of a contract under these provisions is easier by any means as just cause still needs to be shown pursuant to the rules and principles of evidence and court, however there is no disputing the fact that this statutory remedy is available to those who are in dire need of exercising it where a contract can be construed as being unfair. Unfairness may result from the terms of the contract itself, or from any conduct by the creditor arising after the commencement of the agreement, thus this legislation appears to be catering more for the debtor than the creditor. These provisions specifically cover, in their express terms, any unfairness arising from the conduct of the creditor, as does not relate to the debtor as such. When viewed in conjunction with the application and definition provisions outlined above, it is clear that this law only intends to serve the individual, and not the creditor.

In addition to the ‘ unfair relationship’ protection through the courts afforded to debtors by the introduction of the 2006 Act, it also contains an alternative dispute resolution pathway that can often avoid a long and arduous litigation process. Sections 59-61 of the *Consu me r Credit Act 2006* confer powers upon the Financial Services Ombudsman to hear any disputes that involve licensed persons (i. e. a credit provider company licensed under the 2006 Act, which will be discussed shortly), and will also bind these license holders to abide by any decisions made by the FSO in accordance with Schedule 2. Section 59 of the Act requires that any person holding a license to provide consumer credit must submit to the jurisdiction of the Financial Ombudsman Service in order to resolve any disputes which the FOS is empowered by the Act to hear. In order for the dispute to fall within the scope of the jurisdiction of the FOS, it must meet the eligibility criteria outlined in the new section 226A of the *Financial Services and Markets Act 2000* (inserted by the 2006 Act), which are:

(a) the complainant is eligible and wishes to have the complaint dealt with under the scheme;

(b) the complaint falls within a description specified in consumer credit rules;

(c) at the time of the act or omission the respondent was the licensee under a standard licence or was authorised to carry on an activity by virtue of section 34A of the Consumer Credit Act

1974;

(d) the act or omission occurred in the course of a business being carried on by the respondent which was of a type mentioned in subsection (3);

(e) at the time of the act or omission that type of business was specified in an order made by the Secretary of State; and

(f) the complaint cannot be dealt with under the compulsory jurisdiction. [11]

Essentially, if the complaint is one that falls under the compulsory jurisdiction of the Financial Ombudsman Service that is granted under section 226 of the *Financial Services and Markets Act 2000* , then it will not fall under the new consumer credit power. The presence of these provisions makes it more effective and less costly for an aggrieved person to raise a dispute with a consumer credit contract that they have entered, which can (and most likely will) avoid the matter proceeding before a court. This makes the dispute resolution process more accessible for individual persons that may not have otherwise had the available funds to commence a legal action in court.

Finally, the other main practical change that the *Consu me r Credit Act 2006* has made to credit law is the introduction of more stringent licensing criteria for businesses and companies wanting to enter the market to sell credit products to consumers. Section 38 of the 2006 Act inserts a provision in the 1974 Act at section 33A which empowers the Office of Fair Trading to make regulations that will govern the distribution of licenses to these parties. This allows the Government the flexibility to adapt the regulations to address the changing social climate in a way that the broad framework of the 1974 Act could not. This would, then, allow the Government to impose regulations on advertising and other consumer interaction which may otherwise escape the broad legal framework of legislation. Additionally, section 44-46 of the 2006 Act specify requirements in relation to the provision of licensing assessment information (and changes thereof) by license applicants to the OFT, which allows the OFT to make a continual assessment as to the fitness of a party to hold a credit provision license. This was one of the key shortfalls that the White Paper suggested, and appears to have been addressed adequately in the new law. Civil penalties of up to £50, 000 now apply if a licensed person or business fails to comply with the conditions of its credit provision license. [12] Finally, an appeals system has been established by sections 55-58 of the 2006 Act which allow for appeals against a decision by the OFT to grant a license to an applicant, which gives rise to a method of review via the newly established Consumer Credit Appeals Tribunal. This provides for an administrative review of the decisions handed down by the OFT in relation to their licensing and regulative powers within the Act, which may be able to be judicially reviewed by the Court of Appeal with the leave of the Court (on questions of law, not fact). [13] This appeal procedure again appears to be consistent with the notion that the rationale of the C *onsu me r Credit Act 2006* is to protect the rights and interests of debtors as opposed to those of creditors and suppliers. It appears that the idea of this Act is to saturate the market with new regulations that control the way creditors enter into consumer credit contracts with their debtors, and does not necessarily cater for the needs of creditors as such.

In conclusion, it would appear that the *Consu me r Credit Act 2006* caters more so for the rights and interests of debtors than those of creditors, however it would be difficult to maintain an argument to suggest that the law goes too far in protecting these rights. The Government White Paper identified a number of salient points that the 1974 Act did not address, and the Government has appeared to have legislated accordingly. Given that the previous 1974 Act was significantly outdated and not particularly relevant to modern society in both a social and legal context, there was a real need for this law to be updated in order to afford consumers maximum protection against otherwise unfair conduct that was not recognised in law. The law was updated more out of necessity than out of spite for consumer credit providers. The application of these laws does not generally appear to infringe on the rights of credit providers, it merely suggests that the market needs more stringent controls to avoid certain parties taking advantage of otherwise vulnerable individuals. The rationale behind the introduction, as the White Paper suggests, was to create a fairer and more transparent consumer credit market, which gave the individual more competitive and legitimate rights that they are now able to exercise in an attempt to remove the disparity between consumers and credit providers in terms of their negotiation and contractual abilities. There appears to be no malice or ill-will by the Government towards credit providers, rather just a desire to exercise control in an area of commerce that has expanded exponentially since the law was last reviewed more than a generation ago. The flexibility provided under the new Act through delegation of regulative powers to the OFT and Ombudsman also allows the law to be updated as society dictates, which ensures that the law will always be given the opportunity to reflect the needs of consumers as the market changes. This means that this debate will continually be revisited as the market expands and changes and, if there is a need to review the law in the future, there is no need to go through the lengthy legislative process which has dragged this legislation through 18 months of parliamentary delays, especially due to the calling of the 2005 General Election after the Bill was only passed its Commons stages. This law appears to be perfect for the current socio-economic climate of the British consumer credit market, and to argue that it goes too far in protecting consumer's rights is simply untenable.

Bibliography

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Footnotes

[1] Department of Trade and Industry, *Fair, Clear and Competitive: The Consu me r Credit Market in the 21 st Century* (2003), 4.

[2] Ibid, 30-33.

[3] Department of Trade and Industry, as above n 1, 33-36.

[4] Ibid, 37-40.

[5] Ibid, 45-48.

[6] *Consu me r Credit Act 2006* , s 1.

[7] *Consu me r Credit Act 1974* , s 8.

[8] *Consu me r Credit Act 2006* , ss 19-22.

[9] *Consu me r Credit Act 1974* , s 140A(1).

[10] *Consu me r Credit Act 1974* , s 140B(1).

[11] *Consu me r Credit Act 1974* , s 226A(2).

[12] *Consu me r Credit Act 1974* , s 39A (as amended).

[13] *Consu me r Credit Act 1974* , s 41A (as amended).