

07 March 2011

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Dear Ms Ellis

## Consultation response on: Mental capacity – Draft OFT guidance for creditors

The higher incidence of debt problems among people with mental health difficulties is well-documented.<sup>1</sup> Debt-related difficulties can also result in people experiencing a range of mental health problems.<sup>2</sup> Our own research into people without bank accounts found that people with mental health problems frequently experienced serious debt and housing problems.<sup>3</sup> Given the acute difficulties associated with problem debt and mental health, much of the focus in this area has been on what should happen when things go wrong. There has been less consideration in respect of how consumer credit sales at the beginning of the process should be managed. Our research identified that during episodes of mental ill health some consumers took on unaffordable debt and/or inappropriate financial products.<sup>4</sup> The hangover debt from these periods of instability can become a barrier to financial recovery. Therefore, if it were possible to prevent some consumers taking out inappropriate products in the first place, it could save them considerable distress and anxiety, as well as financial difficulties. Thus, this guidance is particularly welcome.

The guidance explains the legal situation in respect of mental capacity clearly. We are concerned, however, that in the desire not to be overly prescriptive and/or to increase the cost and regulatory burden on creditors, the guidance lacks sufficient detail in terms of the types of practices and procedures which would be considered appropriate. For example, creditors are expected to review their practices and procedures in terms of making 'reasonable adjustments' where it is believed or suspected that the borrower has, or may have, 'some form of mental capacity limitation'. This is to enable the borrower to make 'an informed borrowing decision', while ensuring appropriate safeguards are in place. However, little detail is given as to what, in practice, those reasonable adjustments or safeguards might be.

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<sup>1</sup> Mind (2008) *In the red: debt and mental health*, <http://bit.ly/gLHtmQ> (PDF 707KB)

<sup>2</sup> Ibid

<sup>3</sup> Consumer Focus (2010) *On the margins: Society's most vulnerable people and banking exclusion*

<sup>4</sup> Ibid

## Identifying and dealing with mental capacity issues

The guidance makes a distinction between situations where the creditor knows the borrower lacks capacity; where the creditor has reasonable cause to believe the borrower lacks/may lack capacity; and where the creditor has reasonable grounds to suspect that the borrower lacks/may lack capacity. The substantive differences between these situations should be expressed more clearly within the guidance.

We are also concerned about the extent to which it will be possible for assessment of capacity to take place when borrowing decisions are being made online and even, though to a lesser degree, over the telephone.

### Knowing – or having reasonable cause to believe – that a borrower lacks capacity

The guidance states that there ‘are likely to be only limited circumstances in which creditors could reasonably be expected to **know** – or have **reasonable cause to believe** – that an individual lacks the mental capacity to make a lending decision’ (para 3.16 – emphasis as in original document). We are concerned that knowing and, in particular, having ‘reasonable cause to believe’ that an individual lacks capacity, is being expressed too narrowly, by being confined to situations where the lender is told that this is the case by the borrower or a third party, or the borrower is alerted to this by a power of attorney. We would not want lenders to be able to use the absence of these two specific factors in a particular case to claim that they were not in a position to know or have reasonable cause to believe that an individual lacked capacity, when other factors present in the case should have given them sufficient cause.

It is suggested that a borrower is provided with ‘enhanced communication of the key features of credit agreements’, which would present the information in the agreement in a user-friendly way, e.g. in an ‘Easy Read’ format. ‘Enhanced explanations’ are also proposed. It is important to be very cautious in using additional information as a solution. Research by our predecessor organisation, the National Consumer Council, found that overly complex information caused more vulnerable consumers to disengage and that they sometimes found it humiliating that they were unable to grasp the relevant information. If any ‘enhanced’ information was to be provided to consumers who have limited mental capacity, it would need to be drafted by specialists, with relevant consumer input, otherwise it could have the opposite effect to that intended.

In terms of assessing whether an explanation has been sufficient to enable the borrower to make an informed decision, we are, again, concerned about the extent to which this will be realistic through remote channels, particularly online. This is acknowledged in the Irresponsible Lending Guidance (ILG) paragraph 3.6. Thus, with online lending on the increase, the safeguards in place to prevent inappropriate lending to consumers with mental health problems are likely to be very limited.

In paragraph 3.29, it is stated that ‘where a borrower still appears unable to understand, retain, weigh-up the information or communicate his borrowing decision, even after the provision by the creditor of an enhanced explanation, then the creditor will need to consider whether it would be appropriate to provide the borrower with the credit he is seeking under such circumstances’. This does not go far enough. We feel that the guidance should state clearly that this is a situation where providing the borrower with credit would be seen as irresponsible lending, unless the lender was able to provide an explanation as to why the situation was exceptional and lending was justified in the circumstances.

## Reasonable grounds to suspect that a borrower might lack capacity

We agree that when a lender has reasonable grounds to suspect (as opposed to believe) that the borrower may lack capacity they should apply a high degree of scrutiny to the application. This should be the same for consumers who have been able to reach capacity with assistance. However, the lender must not discriminate unlawfully against the applicant on grounds of mental health or disability. If the borrower is to be subject to a more stringent affordability and suitability test, then the guidance is silent as to whether the borrower should be aware of this. In view of the decisions being taken and the potential impact on the borrower, we believe that the lender should disclose that they are taking this approach to the borrower's application and the reasons why. Clearly this will require sensitivity and discretion on the part of the lender and is another reason in support of a specialist team for dealing with such issues (see below).

We agree a primary consideration is whether the credit sought is affordable and suitable for the individual consumer. We consider that the sustainability of borrowing should be assessed according to both financial and personal well-being. Therefore paragraphs 3.56 and 3.67 should be reworded so that they refer to credit being 'unsuitable' rather than 'clearly unsuitable'.

However, although it is essential to assess affordability and suitability, it is also important that a consumer is given an explanation of the credit agreement that they are able to understand. We believe the guidance should require the lender to ensure an informed borrowing decision is made by the borrower. The lender should be required to take steps similar to those required where a borrower's lack of capacity is known or where there are reasonable grounds to believe the borrower lacks capacity.

An issue that we feel is not fully acknowledged within the guidance is the potential conflict when a lender is required to assist with improving a person's capacity and provide them with support through the lending process. The lender has a financial interest in making the sale and it should be acknowledged that therefore it is unlikely to be appropriate for sales staff to assist the consumer with improving their capacity. We therefore strongly endorse the OFT's view in paragraph 3.37 that it would be good practice for lenders to provide dedicated support services for borrowers when there are indications that they lack or may lack capacity. We also believe that it should be good practice for front-line sales staff to receive basic training to enable them to recognise when an issue of capacity arises and when referral to a specialist is needed.

We recognise that this is a complex situation and there will continue to be occasions when lenders will make legitimate decisions to lend to consumers with mental health problems, who subsequently get into problems with debt. It is essential that lenders have in place the full mechanisms for dealing with this situation and use the *Good practice awareness guidelines for consumers with mental health problems and debt* produced by Money Advice Liaison Group<sup>5</sup> (MALG).

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<sup>5</sup> Money Advice Liaison Group (2009, 2<sup>nd</sup> ed) *Good practice awareness guidelines for consumers with mental health problems and debt* <http://bit.ly/ika1pD> (PDF 871KB)

We would also suggest that, if in England and Wales, as in Scotland, a lack of capacity made a contract void, rather than simply voidable, lenders might be more rigorous in the assessment of capacity, when making the decision to lend.

We would welcome the opportunity to discuss any of the issues raised in this consultation response further.

Yours sincerely

Marie Burton

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