Personal Contract Plans: the Irish Market

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Coimisiún um Iomaíocht agus Cosaint Tomhaltóirí
Competition and Consumer Protection Commission

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1. Introduction

Background and Context

1.1 Having originated in the USA and UK, Personal Contract Plans (PCPs) were introduced in Ireland towards the end of the last decade, during the financial crisis, when car[1] manufacturers sought to address a significant drop in sales. The market had collapsed with new car sales falling by 63% in 2009. In addition to lowering the demand for new cars this also led to a scarcity of "younger" second-hand cars in the Irish market as consumers increasingly held on to their cars for longer than had been the case before. By the time many consumers came to trade in, the value of their cars was not enough to provide a sufficient deposit on a new car; for example the price gap between a seven or eight year-old car and a new one was considerable. Against this backdrop, some car manufacturers that offered PCPs elsewhere introduced the products to Ireland. PCPs can address the circumstances in which consumers do not have enough trade-in value to use their car as a deposit for a new one as they generally involve a relatively low upfront deposit, low monthly repayments and a large payment at the end. In effect, the largest financial burden on the consumer is shifted to the future. This can be attractive for a number of reasons as detailed in this study.

1.2 According to data collected for the first time by the Competition and Consumer Protection Commission (CCPC), in 2016 the value of the credit extended to consumers via PCP agreements was approximately €800 million, accounting for just under 33,000 cars.

1.3 In recent years PCPs have attracted considerable attention from consumers who have contacted the CCPC, from public representatives and in the media. The CCPC became increasingly aware of the growth of PCP agreements as a method for financing the purchase of a car[2], the complexity of these agreements and related issues. Such issues included a lack of awareness of certain terms and conditions, uncertainty as to the meaning and effect of certain terms and conditions at the end of agreements, and questions around the regulatory status and protection afforded to consumers.

1.4 Against this background, on 17 July 2017, the CCPC announced that it would undertake a study of the PCP car finance market.

1.5 The study was conducted in order to compile evidence in relation to:

- the size and characteristics of the PCP market;

[1] For ease of use; the term "car" is used in this report. It refers to any vehicle purchased by a consumer.

[2] Between 2015 and 2016, the value of new PCPs issued for new car sales rose by 65%.

- the experience of consumers in the market as well as their ability to understand PCP agreements; and
- the current protections available to consumers under the Consumer Credit Act 1995, as amended[3], referred to henceforth as the CCA 1995.

The evidence compiled is intended to inform any consideration of the market by policymakers and relevant stakeholders. The study specifically considers the potential for consumer risk and detriment, now and in the future, and proposes a range of recommendations, designed to provide greater protection for consumers when they enter into PCP agreements.

Structure

1.6 This study is set out as follows:

- The rest of this Chapter describes the research undertaken by the CCPC and sets out a high level overview of PCP products;
- In Chapter 2 the retail car sales market is described with a specific focus on the evolution and growth of the PCP finance market in Ireland;
- Chapter 3 examines consumers' experiences of PCP products, and assesses the information provided to them at the point-of-sale, the consumers' understanding of PCPs, the structure of the product, and the options available to consumers at the end of the agreement;
- Chapter 4 provides an overview of the current regulatory framework governing the supply of PCP products;
- Chapter 5 contains a summary, conclusions and associated recommendations.

Methodology

1.7 In order to fully understand the operation of the PCP market and ensure that any recommendations are evidence based, the CCPC carried out the following research steps:

- Extensive desk-based research was undertaken into the range and types of PCPs that are available to consumers in Ireland.
- An analysis of relevant legislation was conducted.
- Detailed questionnaires were issued to all financial institutions that underwrite PCP finance. The data which was returned allowed the CCPC

[3] [3] An administrative consolidation of the Consumer Credit Act 1995 is available at http://www.lawreform.ie/_fileupload/RevisedActs/WithAnnotations/EN_ACT_1995_0024.PDF

to compile, for the first time, primary data relating to the number and value of PCP finance contracts issued in the State.

- Detailed questionnaires were issued to all of the car dealer credit intermediaries on the CCPC register, resulting in 85 responses, 61 of which were from car dealers who arrange PCP finance.

- In-depth interviews were conducted with a number of the larger car dealerships in the State.

- Amárach Research was commissioned to undertake a series of focus groups with consumers to examine their understanding and perceptions of the PCP product, their experiences of the PCP sales process and their views on the suitability of the product.

- In addition to a review of the information provided by contacts to the CCPC's consumer helpline, the CCPC requested submissions from individual consumers regarding their views of and experience with PCP products. A total of 17 submissions were received and nine in-depth interviews were conducted.

1.8 It is important to note that this study focuses on the retail sale of new cars to private consumers i.e. business to consumer transactions (referred to alternatively as private new car sales). Some comments are made on the second-hand car market, specifically in relation to the spread of PCPs into this segment of the market. The study does not examine the sale of new cars under a commercial arrangement such as corporate car purchase or leasing schemes, fleet sales or sales to car hire firms.

1.9 Purchasing a car and choosing the method of finance, for most consumers, is a major financial decision. There are a number of different options whereby consumers can finance the purchase of a car; with cash, with a term loan from a bank or credit union, through a standard hire purchase agreement or by entering a PCP finance agreement. PCP agreements are used in Ireland primarily for the purchase of new cars, but increasingly there are opportunities to purchase second-hand cars using PCPs. The context to this financial decision is that many consumers will be focused on choosing a particular car and the decision regarding the method of finance may be secondary. The CCPC conducted research amongst a sample of consumers on this point in 2016. The results found that in terms of the time taken to select the right car, consumers said that they spent an average of 9.7 hours researching at home and 7.2 hours physically viewing cars. By contrast consumers reported that they spent an average of 3.8 hours researching finance options. That is, they spent almost 4½ times longer selecting the car in comparison to considering how to pay for it.[4]

[4] https://www.ccpc.ie/business/wp-content/uploads/sites/3/2018/02/CCPC-Car-Buying-Research-April-2016.pdf

What is a Personal Contract Plan?

1.10 Having considered in detail the relevant legislation it is the CCPC's view that, in the absence of a legislative definition, PCP generally displays the characteristics which one would associate with hire purchase. It is a complex car finance product that has similarities to both consumer hire and a traditional hire purchase, i.e. buying by paying instalments. Unlike most traditional HP agreements, where the total amount borrowed is divided into equal monthly instalments over the term of the agreement, with a nominal additional payment a the end, a PCP is structured differently, with the payment of an initial deposit, followed by a series of low monthly repayments and a large final payment to be made at the end of the agreement.

1.11 As a substantial portion of the amount borrowed is left until the end of the term, the monthly repayments with a PCP can be lower than a standard HP agreement. The CCPC's research suggests that low monthly repayments are one of the attractive characteristics of PCPs for consumers. Lower repayments make new, and more expensive, cars more accessible than is the case with traditional forms of finance.

1.12 In addition, interest rates for PCPs are often substantially less than the interest rates charged on other forms of car finance. Two reasons for this which were highlighted to the CCPC are that PCP lending is secured by the value of the vehicle as collateral and also that car manufacturers are subsidising the interest rates to encourage car sales. CCPC research found that the typical annual percentage rate (APR) on a PCP is between 0% and 5% which is applied to both the monthly repayments and the guaranteed minimum future value (GMFV – see below for an explanation of this term), versus the typical 7% - 10.5% APR for a personal loan[5].

How Does a PCP Work?

1.13 With a PCP, payment for a car is broken down into three parts:

- **The deposit** - is typically between 10% and 30% of the retail price of the car. The deposit can be paid in cash or if the consumer already owns a car, s/he can trade this in for part or all of the deposit, depending on its value.

- **Monthly repayments** - PCP contracts typically have a duration of 36 months[6]. They generally have lower monthly repayments compared to HP or personal loans, because they do not cover the whole cost of the car. Rather, during the course of the PCP the consumer pays the difference between the value of the car at the time of purchase and the Guaranteed Minimum Future Value (GMFV), explained further below.

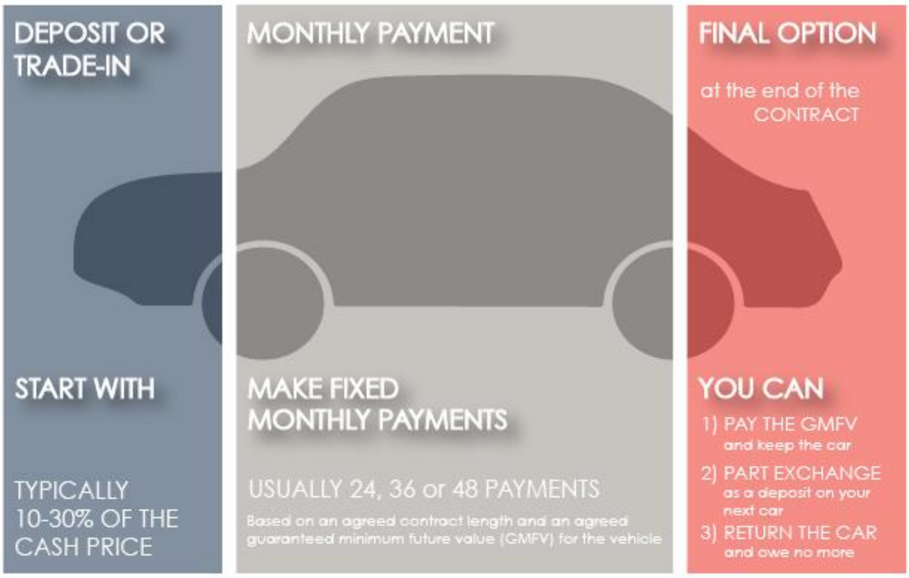
[5] Source CCPC Financial Product Comparisons as at 12 February 2018.

[6] PCPs can also be structured over 24 or 48 months

Effectively the deposit and the monthly payments cover the cost of the car's depreciation together with some additional equity to cover fluctuations in the market. When the GMFV is set at the beginning of the contract it should be lower than the expected retail price of the car when the term ends. Therefore, ideally there should be some equity in the car which can be used towards the next PCP if the consumer wishes to enter a new agreement. If however the value of second-hand cars falls in the period of the PCP agreement, then the consumer may not have any equity in the car at the end of the agreement.

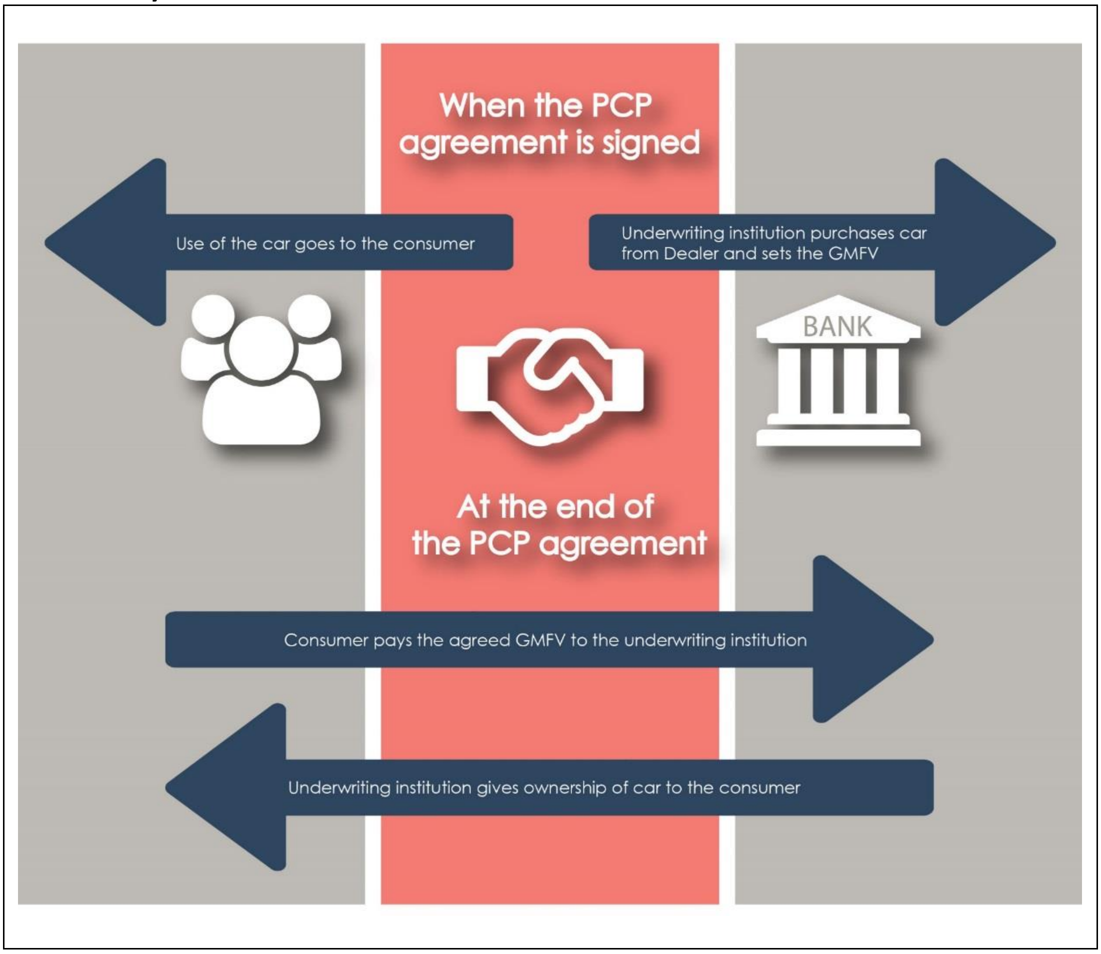
- **Guaranteed Minimum Future Value (GMFV)** - A portion of the car's value is deferred until the end of the agreement. This large, final payment is what the financial institution estimates will be the value of the car at the end of the contract. The GMFV is set by the financial institution that underwrites the PCP. The GMFV is also referred to as a balloon payment.

Figure 1.1 How PCPs work



1.14 Generally speaking, the GMFV is set by the financial institution that underwrites the PCP so that it will be lower than the forecasted market value of the vehicle at the end of the contract. The reason for this is twofold; (i) to allow for potential market fluctuations; and (ii) to allow the consumer to build up equity in the car, which may then be used as a deposit on a subsequent PCP. This means that PCP finance is particularly susceptible to changes in the value of second-hand vehicles, an issue which is examined in more detail later.

Figure 1.2 PCPs – Relationships between the Consumer, the Credit Intermediary and the Credit Institution



1.15 At the end of the PCP contract the consumer has three options to choose from:

- **Hand the car back** and walk away - Importantly, handing the car back without making additional payments to the dealership, is subject to meeting all the terms and conditions. For example, there are penalties for exceeding any mileage restrictions or excessive wear and tear on the car.

- **Pay the GMFV to own the car** - The car only becomes the property of the consumer once the final payment (i.e. the GMFV) is made. It should be noted that in addition to this payment, there may be other fees associated with buying the car, for example acceptance fees or completion fees. These should be outlined in the PCP contract at the outset. It is also noteworthy that it may be possible to refinance the GMFV if necessary.[7]

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[7] The CCPC's consumer research indicated that saving for the GMFV at the start of the period was not considered a priority by consumers. As a result, the majority of consumers who, for whatever

'Roll' the PCP contract – This means that the consumer enters a new PCP agreement for another vehicle. The GMFV is usually set at a value lower than the expected open market value which means that consumers can use the difference towards a deposit on a new car that is financed by a new PCP agreement. The CCPC's consumer research found that the majority of consumers enter their initial PCP agreement with a view to availing of this option at the end of term.

If at the end of a PCP agreement an owner wants to roll their PCP, the condition of the car becomes a contributing factor to the car's value. Therefore, in this instance, the GMFV is subject to terms and conditions such as, wear and tear and mileage restrictions, which are set out at the start of the contract.

1.16 It is the CCPC's view that these products are complex, not least given the number of variables and alternatives which the consumer has to consider and forecast at the outset when making an agreement.

1.17 Importantly during the PCP contract, the consumer does not own the car. In contrast to financing a car using a personal loan the car is not the consumer's to sell if they get into financial difficulty and can no longer afford the repayments. The financial institution that underwrites the PCP is the owner of the car. **It is not until the end of the contract that the consumer has the opportunity to buy the car outright.**

Credit Intermediaries

1.18 Consumers will often enter a PCP agreement through a credit intermediary. *"Credit intermediary means a person, other than a credit institution or a mortgage lender, who in the course of his business arranges or offers to arrange for a consumer the provision of credit or the letting of goods in return for a commission, payment or consideration of any kind from the provider of the credit or the owner, as the case may be"* (CCA 1995). Examples of credit intermediaries are garages and high street retailers, such as furniture and electrical retailers, leasing or hiring out goods or selling on credit or arranging credit finance provided by credit institutions[8].

1.19 A credit intermediary can arrange or offer to arrange a PCP for a consumer. The CCPC is responsible, under the CCA 1995[9], for the authorisation of credit intermediaries, some of whom sell PCPs to consumers on behalf of financial institutions. The CCPC licenses credit intermediaries and keeps an online register of credit intermediaries holding a valid authorisation. The CCPC also deals with complaints about the advertising of credit agreements. However, the CCPC's

reason, wanted to buy the car at the end of term, refinanced the GMFV. Many dealers offer to refinance the GMFV under a standard HP agreement.

[8] See https://www.ccpc.ie/business/credit-intermediaries/advertising-credit-facilities-authorising-credit-intermediaries/

remit is limited to this licensing role, as opposed to a more complex and robust regulatory role.[10]

1.20 While the majority of the financial institutions that offer PCP finance through credit intermediaries are already regulated by the Central Bank, the Central Bank's Consumer Protection Code (the Code) does not currently apply to hire purchase (HP) products or variants thereof such as PCPs. This is significant as Chapter 5 of the Code requires regulated financial services providers to "know their customer" in terms of assessing the affordability and suitability of products covered by the Code.

1.21 Normally, when a consumer is offered a PCP, the agreement is arranged by the car dealer who is acting as a credit intermediary for finance providers such as manufacturer banks or the car finance arms of the main retail banks.

1.22 Issues in relation to authorisation and regulation are discussed at length in Chapter 4.

The Nature of the Agreement

1.23 When a PCP is chosen by the consumer to finance the purchase of a car, the dealership can be considered as providing two products to the consumer; the asset (the car) and, acting as a credit intermediary, the credit on behalf of the credit institution (the PCP finance).

1.24 Title in the car (legal ownership of the car) remains with the credit institution that provided the finance to the consumer throughout the term of the PCP contract. Legal ownership of the car does not pass to the consumer unless and until the consumer pays the final payment (the GMFV). The credit institution's ownership of the car should be noted in the car's history whenever anyone inspects it, so a consumer cannot sell the car without clearing the finance first.

1.25 In the next chapter there is an overview of the retail private car sales market and an examination of the PCP market including its size, value and some of the associated product risks.

[10] It is equally important to note that the CCPC does not have a remit with regard to the prudential regulation of the financial institutions that underwrite PCP finance. Prudential regulation for regulated financial institutions is within the remit of the Central Bank of Ireland and this matter is therefore not considered further in this report.

2. The Private Car Sales Market: An Overview

Introduction

2.1 This chapter provides an overview of the main characteristics of the private car sales market in Ireland. In addition to a general overview of the new and used car markets and an analysis of the dealership structure, this chapter presents a detailed examination of the PCP market. This represents the first public analysis of the PCP market in Ireland.

2.2 PCP finance has grown significantly in Ireland in recent years, with the number of new PCPs issued increasing from 21,000 in 2015 to just under 33,000 in 2016. The value of new PCP finance in 2016 was approximately €800 million, which represents an increase of 65% when compared to 2015. The growth in PCP finance partially reflects a recovery in the new and used car markets, as well as a change in how private new cars are purchased with PCP used to purchase an estimated 30% - 34% of all private new cars in Ireland purchased by consumers.

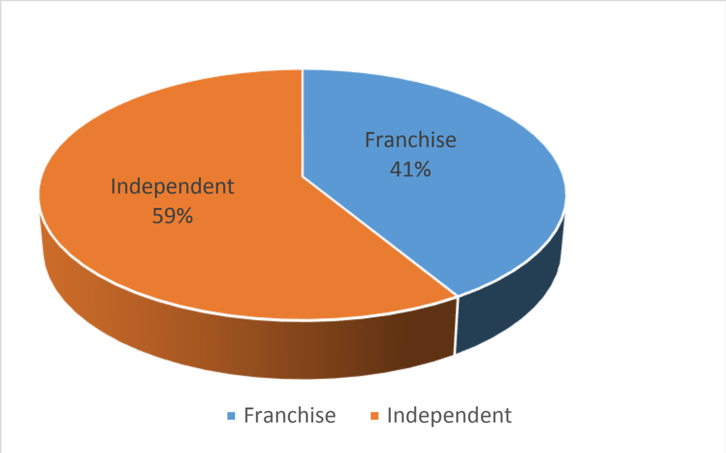
2.3 This chapter uses information obtained from the Central Statistics Office (CSO), the Central Bank, the Society of the Irish Motor Industry (SIMI) and the financial institutions that underwrite PCP finance to provide a detailed analysis of the PCP market.

Dealership Structure

2.4 To date, PCPs have primarily been used when consumers are purchasing new cars, although the market is expanding into the second-hand market. New cars are sold almost exclusively by franchised dealerships in Ireland[11]. A franchised dealership is a car seller that sells new and used cars for car manufacturers. The manufacturer is often listed in the dealership's name. Independent dealerships on the other hand have no affiliation with the manufacturers and usually specialise in the sale of used cars. There are currently 429 franchised dealerships in Ireland.[12]

[11] Independent dealers are free to buy new vehicles from franchised dealers for re-sale.
[12] Over 95% of franchised dealerships are SIMI members.

Figure 2.1 Car Dealership Structure in the State, 2016



Source: CCPC analysis of SIMI membership data

2.5 Given that franchised dealerships are the primary sellers of PCP finance in Ireland, figure 2.2 provides an overview of the franchised dealership market and the number of franchised dealerships for each of Ireland's top ten car brands, which together make up over 70% of the new car market.

Figure 2.2 Franchised Dealership Numbers in the State, 2017

Audi	9
Ford	49
Hyundai	25
Kia	29
Nissan	36
Opel	31
Renault	26
Skoda	25
Toyota	43
Volkswagen (VW)	38

Source: CCPC analysis of SIMI data

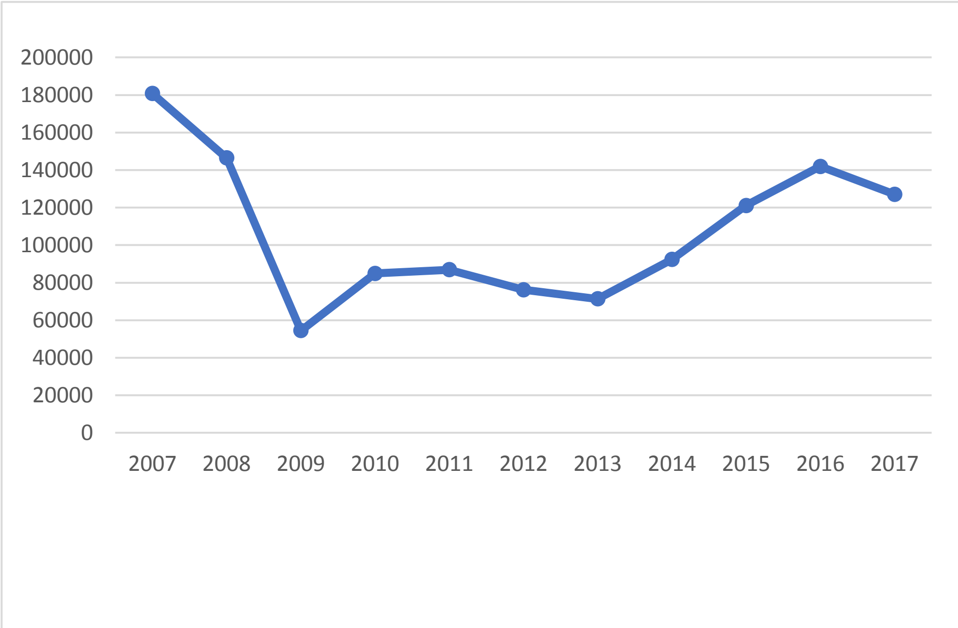
2.6 Some dealerships sell multiple brands. This is the route to market for smaller car manufacturers who do not have the market power to demand exclusivity from dealerships. It is also common for large manufacturers such as VW to have dealerships that stock multiple brands as the VW group owns Volkswagen, Skoda, Seat, Audi and Porsche.

Overview of Trends in Car Sales

New Car Sales

2.7 When discussing trends in the sale of new cars, it should be noted that licensing and registration are different processes. A vehicle is licensed when a valid motor tax disc is issued for the first time, whereas registration occurs when a vehicle gets its licence plate (registration number) for the first time. The total number of cars licensed tends to be slightly lower than total cars registered. However, they both accurately capture trends in total car sales.

Figure 2.3 New Private Cars Licenced in the State, 2007-2017



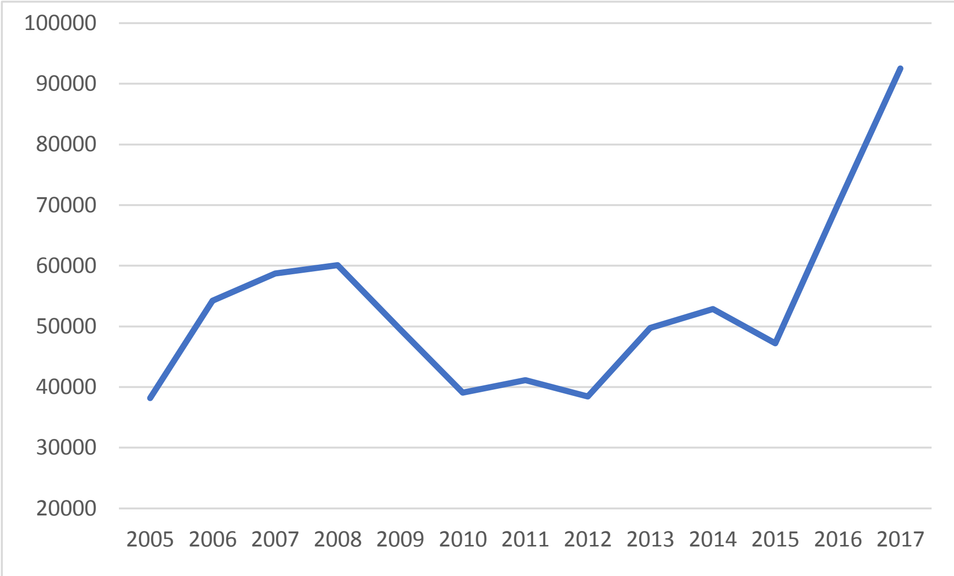
Source: CCPC analysis of CSO data

2.8 Figure 2.3 above presents new private cars licenced for the first time in Ireland from 2007-2017. The graph highlights the significant negative impact which the financial crisis had on new car sales in the late 2000s. The number of new cars licenced for the first time fell by nearly 63% from approximately 143,000 in 2008 to 54,000 in 2009, before gradually rising to a post-financial crisis peak of just under 142,000 in 2016. As can be seen, new cars licenced in 2017 are down by approximately 10% when compared to 2016.

Second-hand Car Sales

2.9 Figure 2.5 presents the number of imported second-hand cars licensed in Ireland for the first time. This shows an increase of over 95% from 2015 to 2017 from approximately 47,000 to 92,500 second-hand car imports.

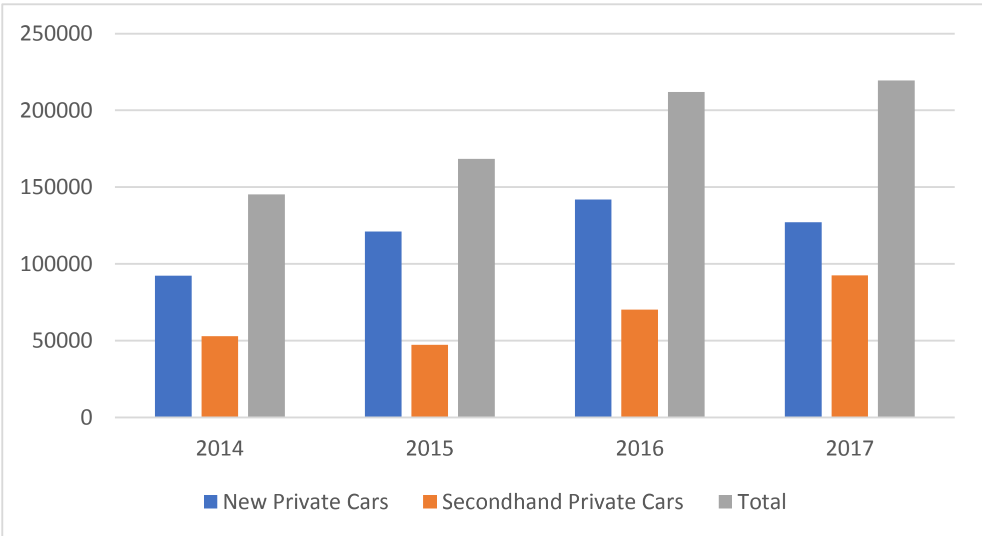
Figure 2.5 Second-hand Cars Licenced in the State, 2005-2017



Source: CCPC analysis of CSO data

2.10 It is likely that the reduction in the number of new car sales in Ireland in 2017 is due in part to the increase in used car imports. An analysis of exchange rate trends and their impact on used car imports is outlined at 2.13, below. Should this trend continue it could represent a risk in the PCP market if the increased supply of second-hand vehicles reduces the value of used cars. However, the impact of increased used car imports on second-hand car values to date is unclear.

Figure 2.6 Cars Licenced in the State 2014-2017



Source: CCPC analysis of CSO data

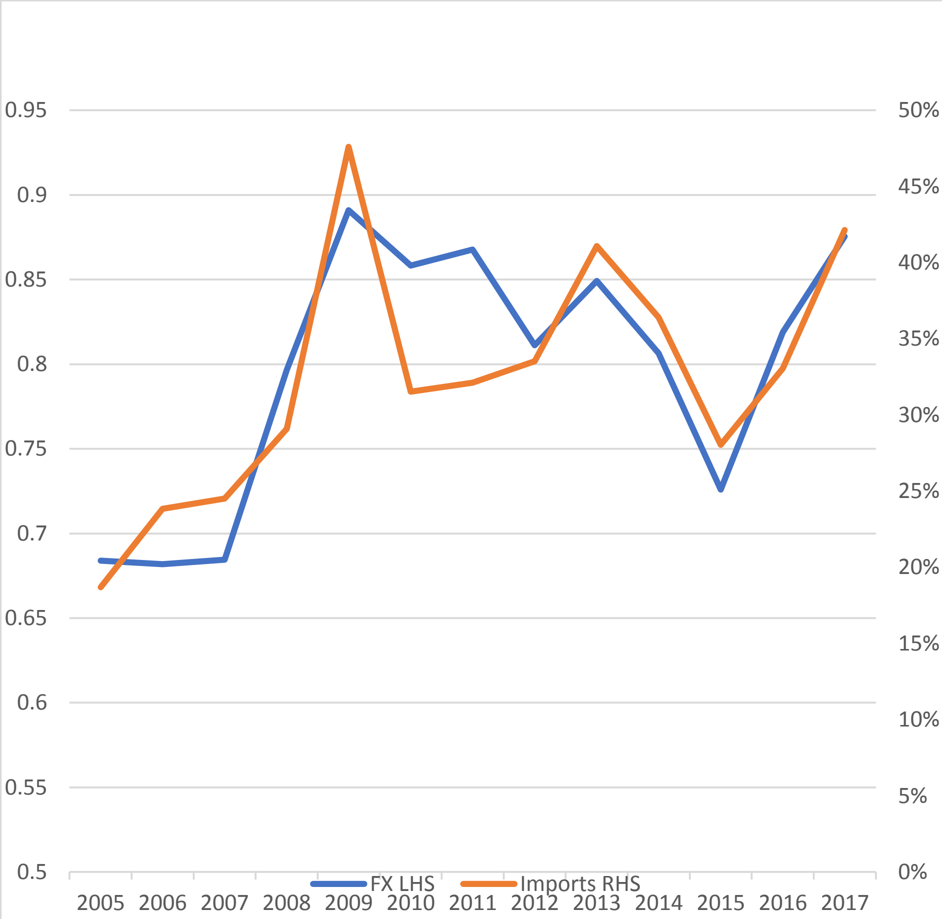
2.11 Figure 2.6 shows (i) total, (ii) new, and (iii) second-hand cars licensed in the State for the first time from 2014-2017. As can be seen, total cars licensed for the first time in 2017 (both new and second-hand) totalled approximately 220,000, up 3.5% from 2016.

2.12 In 2017, 97%[13] of all second-hand vehicles registered for the first time in the State were imported from the UK. Demand for used cars in Ireland is sensitive to fluctuations in the Sterling-euro exchange rate. Used car imports from the UK will be relatively cheaper if Sterling depreciates in value relative to the euro.

2.13 Following from 2.12, Figure 2.7 shows the amount of sterling needed to purchase 1 euro – this figure is shown on the left-hand scale. The right-hand scale shows the level of second-hand car imports as a percentage of total cars licensed for the first time in the State from 2005-2017. The sterling-euro exchange rate closely matches trends observed in the second-hand car import market, although it should be noted that this may not mean that there is a direct causation. As the value of the euro relative to sterling increased between 2005 and 2009, the price of second-hand vehicle imports became more favourable and the number of second-hand car imports as a proportion of total car sales increased. From 2015 to 2017, the value of the euro relative to that of sterling increased by over 20%. This was followed by a 95% increase in the number of used cars imported into Ireland. Going forward there must be considerable uncertainly around the number of second hand cars which will be imported into Ireland and in turn second hand car values, not least because of Brexit. There may be other factors such as a reduction in demand for diesel cars which could also impact on second hand car values. This may have implications for consumers in terms of the amount of equity in the car, if any, that is left at the end of their agreements. It is further suggested that if second-hand car values fell significantly, there may be a negative impact on the car dealers more widely if values fall below the figures committed to under the GMFVs.

[13] SIMI Internal database.

Figure 2.7 Sterling-Euro Exchange Rate and Used Car Imports as a % of Total Cars Licensed for the First Time in the State



Source: CCPC analysis of Central Bank and CSO data

The PCP Market

2.15 The PCP market has grown significantly in recent years. Prior to this study there was no publicly available data on the number or value of PCP contracts that have been issued in Ireland. The CCPC has compiled information from a survey of the financial institutions who underwrite PCP finance in Ireland.

2.16 PCP finance is underwritten by financial institutions ("high-street" banks), manufacturer banks and special purpose institutions which exclusively offer car finance. Dealerships may act as credit intermediaries on behalf of these institutions. None of the financial institutions which sell PCPs offer them directly to consumers.

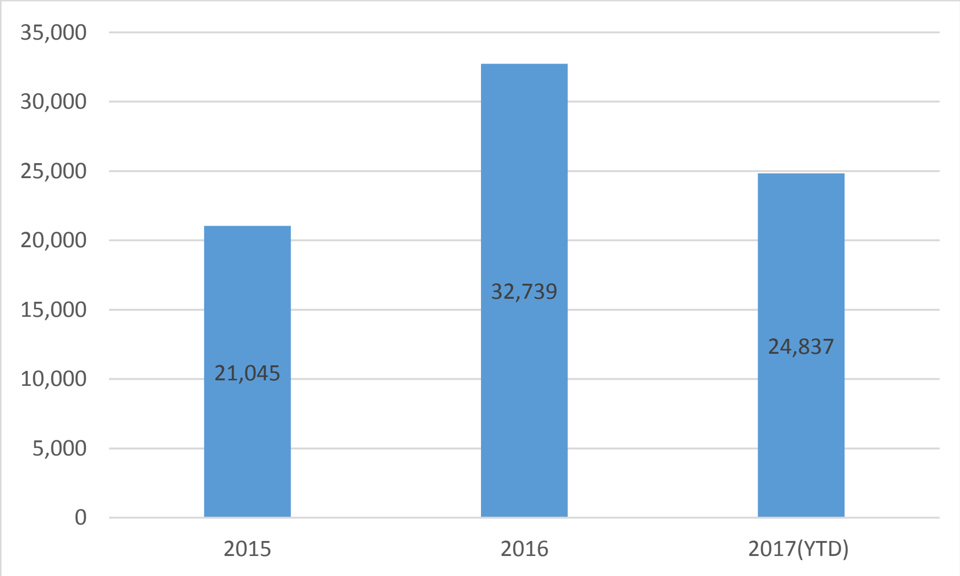
2.17 All of the financial institutions surveyed by the CCPC as part of this study stated that they control the calculation of the GMFV for PCP contracts. As per Chapter 1, the GMFV is based on the estimated future market value of the car. However, most financial institutions discount this value to ensure that (a) consumers will have some equity left in the car at the end of the contract and (b), the dealer/manufacturer bank is not overly exposed to deviations in the value of second-hand cars.

2.18 On the basis of information provided to the CCPC by PCP providers in Ireland, when a PCP agreement is underwritten by a financial institution or specialist motor finance provider, the dealer is liable for any shortfall between the GMFV and the market value of the car in the event that the consumer hands it back at the end of the contract. In contrast, if a PCP is underwritten by a manufacturer bank, the manufacturer bank is liable for the shortfall between the GMFV and the market value of the car. This point is significant in determining where the potential risk lies in a scenario where there is a significant downturn in the market for second hand cars.

2.19 Interest rates for the vast majority of PCP contracts issued are subsidised by car manufacturers, either directly through their own manufacturer bank or indirectly through agreements with retail banks and financial institutions. This encourages new car sales and in many cases the APR on PCPs can be as low as 0%.

PCP Market Size – Value and Volume

Figure 2.8 Total Number of PCPs Issued by Year for both New and Second-hand Cars, 2015-2017 (YTD[14])



Source: CCPC analysis of surveyed financial institutions' data

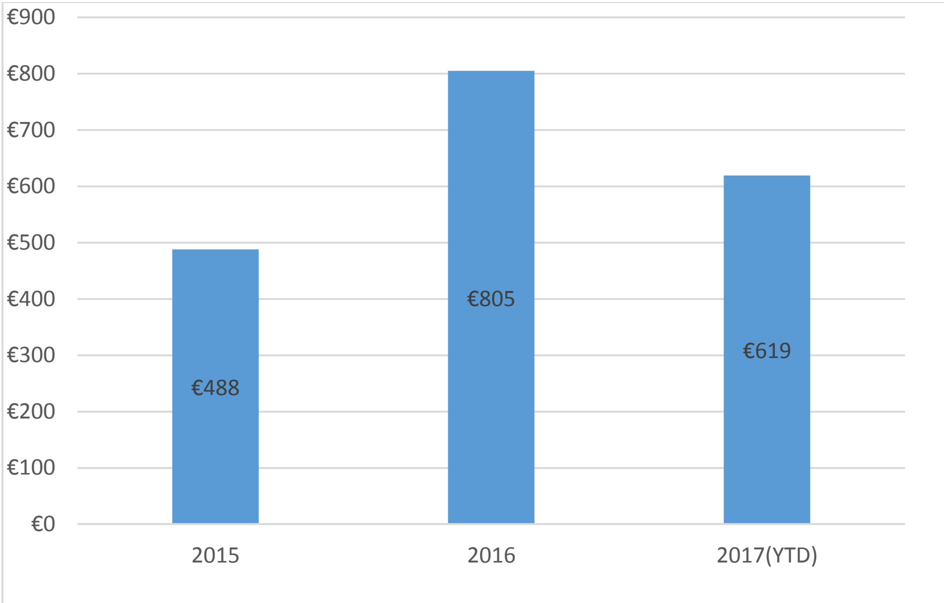
2.20 Figure 2.8 shows that the number of cars purchased using PCPs in 2016 was just under 33,000. The number of PCP contracts issued increased by 55% from 2015-

[14] YTD is as at 1st August 2017 which was the period which the CCPC sought data from when it surveyed financial institutions in late September, early October. Note the other figures for 2017 are for the full year.

2016. The total number of PCPs issued as at 1 August 2017 indicated that total 2017 numbers will be slightly lower than for 2016. This is mainly due to the reduction in new car sales in 2017.

2.21 The total value of PCP finance grew by 65% from €488 million in 2015 to €805 million in 2016. The average PCP contract was worth just under €25,000 in 2016 which implies an average car value of approximately €31,000, assuming an average 20% deposit.

Figure 2.9 Total Value of PCP Market (€m), 2015-2017 (YTD[15])

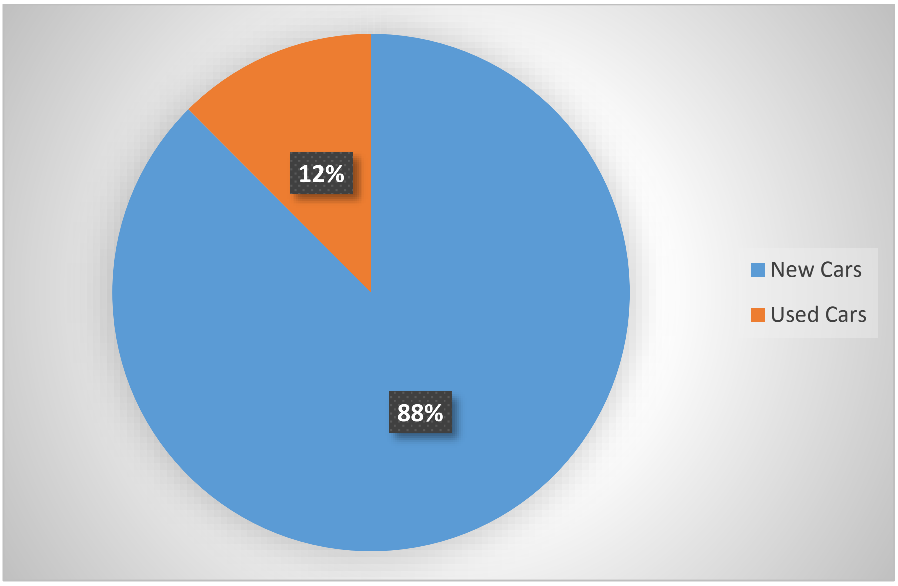


Source: CCPC analysis of surveyed financial institutions' data

2.22 The majority of PCP contracts are for new cars, with 88% of the PCP contracts issued in 2016 for new car purchases. Although it is still a relatively small part of the PCP market (figure 2.10) the number of PCP contracts for second-hand cars increased from 2,038 in 2015 to 4,084 in 2016, an increase of over 100%. This could represent a new growth market for PCP finance providers especially if the number of new car sales continues to decline.

[15] YTD is as at 1st August 2017.

Figure 2.10 Proportion of New and Second-hand Car PCPs issued in 2016



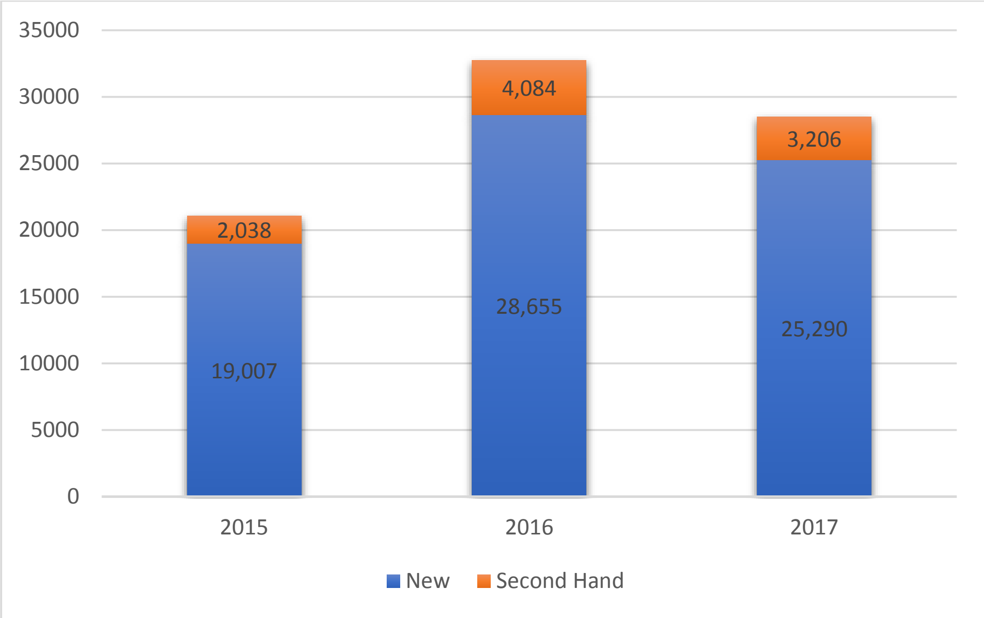
Source: CCPC analysis of surveyed financial institutions' data

2.23 Figure 2.11 presents the total number of PCPs issued in each year from 2015 to 2017 for the purchase of private new cars and private second hand cars. The 2017 figure for new car PCPs is a full year forecast based upon actual PCP figures supplied as at August 2017[16]. However, PCPs used to purchase second-hand vehicles could not be forecasted for the remainder of 2017. As above, the number of PCPs issued for new car purchases in 2017 is forecasted to be slightly lower than 2016.

2.24 It can be seen that the data is quite volatile from year to year, depending largely on the number of new car sales.

[16] This forecast applied the proportion of new cars purchased using PCPs from Jan-August to total new car sales in 2017.

Figure 2.11 PCPs from 2015-2017



Source: CCPC analysis of surveyed financial institutions' data.[17]

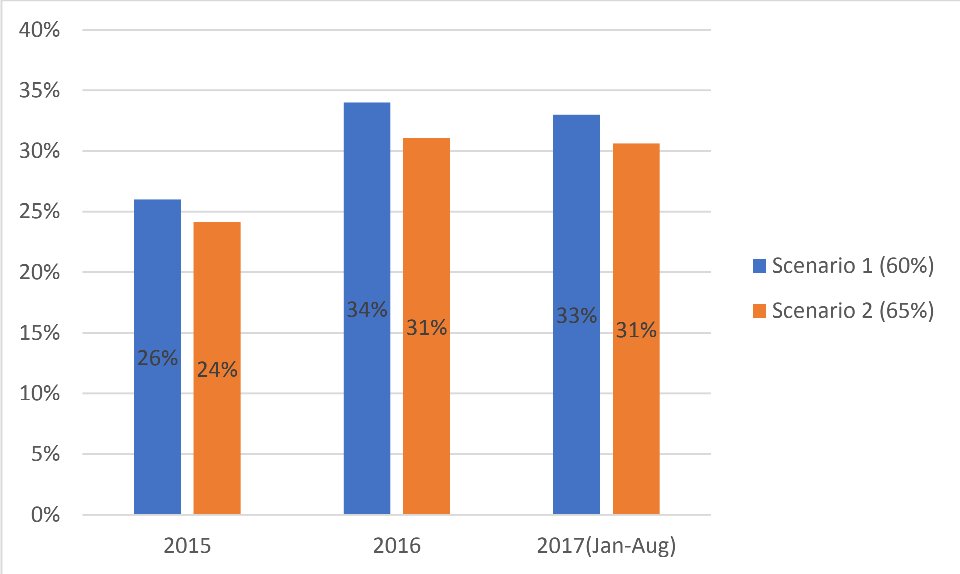
PCP Market Penetration

2.25 The penetration of PCP finance products refers to the incidence of PCP as a form of financing new car purchases when compared to other forms of finance, such as traditional HP and term loans. Assessing PCP penetration using the reported total of new car sales in the State will result in an unrealistically low PCP penetration rate since new car sale statistics include purchases by traders, fleet purchases, pre-registrations by car dealerships, and "demos"[18], all of which are not purchased by private consumers. It is therefore important to estimate the number of new car sales which fall under these categories so that a more representative figure is provided for the total number of new cars sold to private consumers.

2.26 The CCPC has obtained estimates from a number of sources including the CSO and SIMI as well as a number of large car dealers on the number of new cars that are purchased by consumers each year. The figures obtained indicate that the number of new cars which are purchased by consumers is between 60% and 67% of total new car sales. Using this range has allowed the CCPC to estimate a more realistic figure for PCP penetration in the State (see figure 2.12).

[17] Note: for 2017, new car PCPs are forecasted based on data as at 1 August 2017 and projected new-car sales to the end of the year. A similar forecast is not possible for second-hand PCPs and as such, the 2017 figure for second-hand PCPs is an actual figure at 1 August 2017.
[18] Demos are new cars that have been driven by the dealership's staff or as test-drive vehicles.

Figure 2.12 PCP Penetration in New Private Car Sales in the State, 2015 to 2017 (YTD[19])



Source: CCPC analysis of surveyed financial institutions' data

2.27 Figure 2.12 presents the percentage of new cars purchased by consumers using PCP finance under two different scenarios. Scenario 1 is based on consumers buying 60% of new cars, while scenario 2 is based on consumers buying 65% of new cars. The results indicate that for 2016, PCP was used in between 31% and 34% of new car sales. For January-August 2017, this figure was between 31% and 33%.

2.28 While it is difficult to estimate the proportion of second-hand car purchases which use PCP finance, the data as described in 2.22 earlier, suggests strong growth, with the market growing by over 100% between 2015 and 2016 (total second-hand cars purchased using PCP contracts increased from 2,038 in 2015 to 4,084 in 2016). Second-hand PCP finance has, to date, been generally restricted to cars less than 3 years old. However, the growth in the new car PCP market is likely to fuel further growth in the second-hand PCP market as consumers come to the end of their PCPs and instead of purchasing the car, roll to a new PCP contract, increasing the supply of second-hand cars.

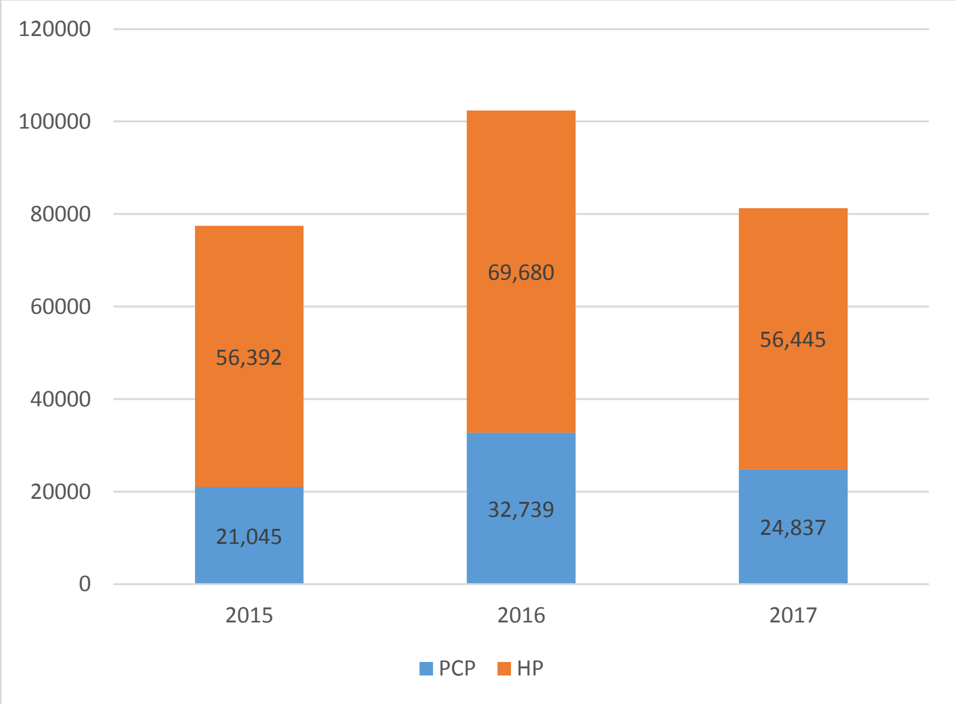
PCP versus Traditional Hire Purchase

2.29 Traditional Hire Purchase (HP) agreements have been a common method to purchase new and used cars. While PCP finance is less common in Ireland than it is in the UK, analysis of new and used car purchases in car dealerships in March 2017 by automotive retail software firm enquiryMAX found that 47.6% of new car buyers and 25.4% of used car buyers used PCP to finance their car purchase[20]. It is likely, given current trends, that the number of consumers availing of PCP

[19] YTD is as at 1st August 2017.
[20] PCPs prevalent in March, says enquiryMAX article 18 April 2017 http://www.am-online.com/news/finance/2017/04/18/pcps-prevalent-in-march-says-enquirymax

finance will, in time, surpass the number of consumers using standard HP agreements to finance car purchases. In 2016 there were nearly 70,000 standard HP agreements issued in Ireland for the purchase of cars amounting to over €1.1 billion, compared to just under 33,000 PCP agreements (see figure 2.13).

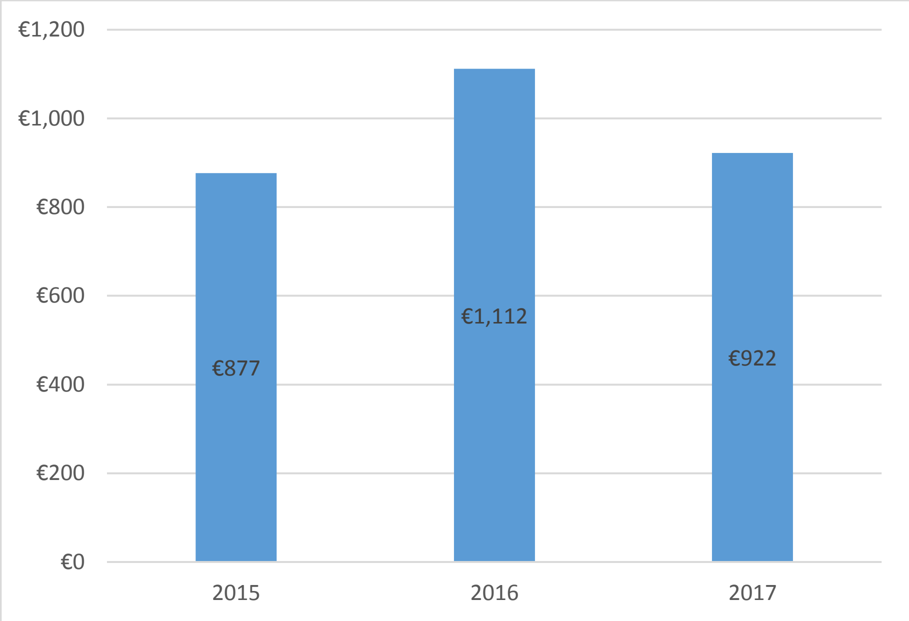
Figure 2.13 Total PCPs and Standard HPs Issued in 2015, 2016 and 2017 (YTD)



Source: CCPC analysis of surveyed financial institutions' data

2.30 Between 2015 and 2016 the total value of the standard HP finance market grew by 27%, from €877 million to €1.12 billion. The data suggests that the average value of a standard HP agreement in 2016 was €15,900. However, it is not possible to determine the average vehicle value from the data as standard HP agreement deposits vary significantly by contract.

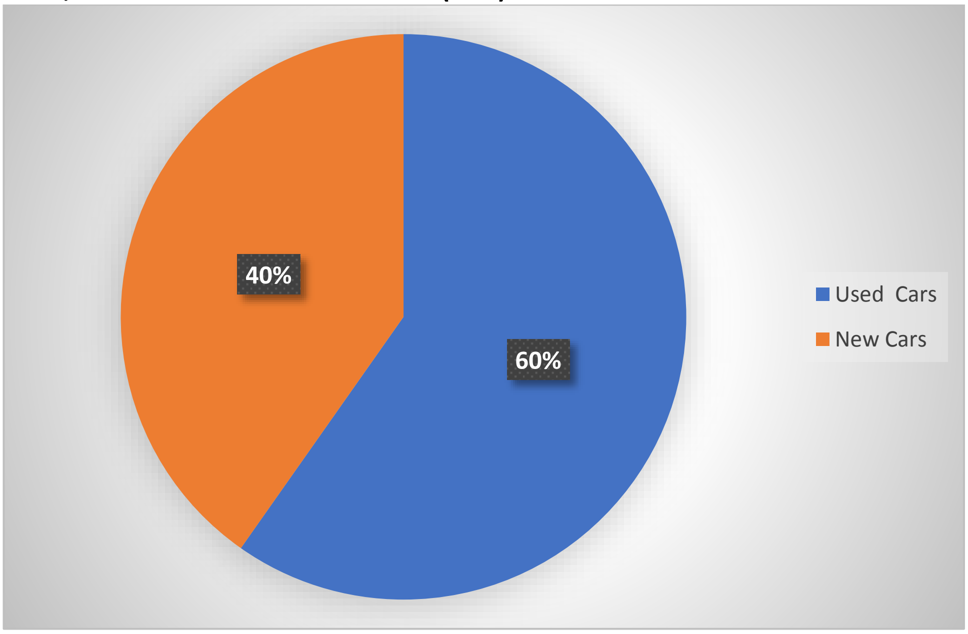
Figure 2.14 Total Value (€m) of Standard HP Car Finance, 2015-2017



Source: CCPC analysis of surveyed financial institutions' data

2.31 The majority of standard HP agreements are for second-hand vehicles with approximately 60% of HP agreements issued for second-hand cars in the period 2015 to 2017 (YTD).

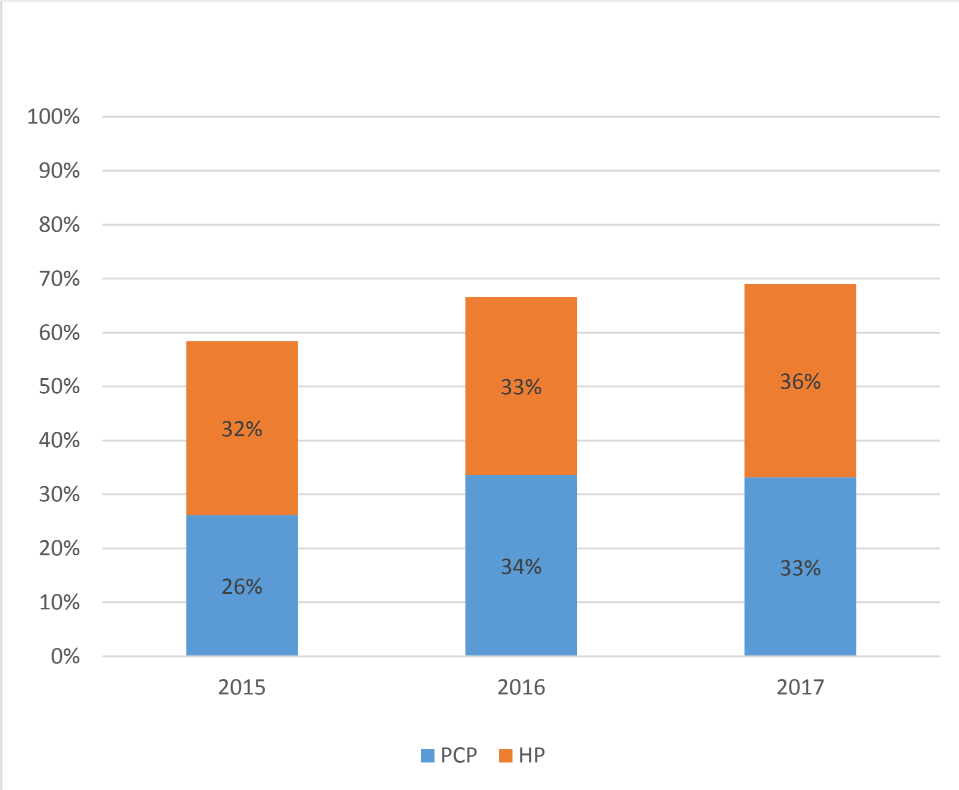
Figure 2.15 Standard HP Market Value Percentage by New and Second-hand Cars, Total for Period 2015 to 2017 (YTD)



Source: CCPC analysis of surveyed financial institutions' data

2.32 Figure 2.16 shows the proportion of new car sales to consumers[21] purchased through both standard HP agreements and PCP agreements. In 2016, approximately 67% of new cars were purchased using either standard HP or PCPs in Ireland[22].

Figure 2.16 Proportion of Private New Car Sales using Standard HP Agreements and PCP Agreements, 2015-2017



Source: CCPC analysis of surveyed financial institutions' data

Analysis of Current Arrears and Default Rates

2.33 Dealership finance and in particular PCP finance has been growing rapidly in recent years. This reflects a recovery in the new car market, as well as a shift in how consumers are purchasing new vehicles.

2.34 The level of PCP contracts that fell into arrears from 2015-2017 (as of 1 August 2017) was low (1.4%) and the default rate over the same period was 0.3%.

2.35 To date, the level of arrears and defaults on PCP finance have been much lower than other forms of household finance in Ireland, with 8.3 per cent of all

[21] It was assumed that 60% of new car sales are consumer purchases.
[22] Assuming 60% of reported new car sales are sold to private consumers.

residential mortgage loans in arrears of over 90 days, and the percentage of non-performing consumer loans at 12.4 per cent as of Q2 2017.[23]

Table 2.1 PCP Default and Arrears Rates (%), 2015-2017 (YTD)

Year	2015	2016	2017 (YTD[24])
Arrears	1.1%	1.2%	2.0%
Defaults	0.4%	0.3%	0.2%

Source: CCPC analysis of credit institution data

2.36 The financial institutions underwriting PCPs were surveyed by the CCPC and the majority did not confirm that they consistently perform standard detailed affordability checks (for either monthly repayments or the final GMFV payment) on potential PCP clients. Some consumers may therefore end up committed to a financial product that is not suited to their means and are therefore running a risk that they will not be able to meet their commitments under the PCP.

2.37 64% of the dealers surveyed said that their sales personnel attend training on PCP products provided by the finance houses. This raises questions about the ability of some dealers to assess customer needs, attitude to risk and suitability.

[23] Central Bank 'Household Credit Market report H" 2017" pg. 16 par 1 and pg.24 par 1.
[24] YTD is as at 1st August 2017.

3. PCP Car Finance: The Consumer Perspective

Introduction

3.1 This chapter presents an overview of PCP car finance products from the perspective of the consumer. Building on the description of PCPs from Chapter 1, this chapter outlines the pros and cons of PCPs and explores consumers' views of the product.

Why PCPs are Attractive to Consumers

3.2 Chapter 1 outlined what PCPs are and how they work. From a consumer perspective, there are a number of features of PCPs that make them a particularly attractive method of financing a car:

- PCPs are relatively cheap to enter at the outset. Initial deposits are low, ranging from 10% to 30% of the value of the car, which means that the consumer, in many cases, only needs a minimal deposit to enter the agreement.

- PCPs generally have lower monthly repayments than other forms of finance. Low monthly repayments coupled with a low deposit means that consumers can access cars that were previously out of their price range.

- PCPs offer consumers an alternative to personal loans to finance the purchase of a new car. This alternative is particularly attractive for consumers who may have difficulty getting approval for a personal loan. This issue alone is very significant in terms of the potential for over-indebtedness, particularly when combined with other financial product commitments. This issue will discussed further in Chapter 5.

- A consumer who has saved to fund the purchase of a second-hand car could find that instead of buying a second-hand car outright, they can use that money as a deposit for a PCP – meaning they can drive away in a brand new car rather than a second-hand one.

- At the end of a PCP agreement, to date, there is usually some equity in the car which can help partially fund the purchase of another car in future.

PCPs: What Should Consumers be Aware of?

3.3 PCPs have a number of appealing features, but as with any financial product, knowledge of all costs, risks and benefits is required to make an informed decision. In this context PCPs have a number of unique characteristics:

- The consumer does not own the car until the final, usually large, GMFV payment is made to the financial institution underwriting the PCP. Therefore until such a point when the final payment is made, the consumer is essentially hiring the car.

- If the GMFV is above or equal to the market value of the car, then there is no equity left in the car. If it had been the consumer's intention to enter a new agreement, then they would have to fund a deposit for the next car purchase from another source.

- The low monthly repayments, while making new cars appear affordable, may in some cases cause consumers to enter contracts which may become unaffordable when the final payment is taken into account. In the CCPC's view, there is potential for detriment in the absence of mandated affordability or suitability checks, particularly given the complexity of PCP products.

- Since a large part of the appeal of PCPs is the low monthly repayment, consumers may be inclined to use a large initial deposit in order to further lower their monthly repayments. However, using a large deposit does not affect either the GMFV, the second-hand value of the car or the final equity in the car which is unlikely to be large enough to allow the consumer to roll to a subsequent PCP with similarly low monthly repayments.

- There are mileage restrictions, wear and tear conditions and crash damage conditions that may incur penalties for the consumer and can affect the amount of equity in the car.

- PCPs display many of the characteristics of hire purchase. However, the fundamental difference in terms of the structure, with PCP deferring a larger proportion of the cost to the end of the agreement, has implications for the protections available to consumers. The CCA 1995 affords consumers important protections in the form of the third[25] and half[26] rules. The structure of a PCP means that it takes the consumer longer to reach the point where they have paid a third or half of the hire purchase price, thus these protections are less relevant.

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[25] Under Section 64 of the CCA, if a consumer has paid more than one-third of the hire purchase price, a lender cannot repossess the car without taking legal action against them.

[26] Section 63 of the CCA allows consumers to end their HP contract, and return the car and they are liable to pay only half of the HP price.

Consumer Understanding of PCPs

3.4 The CCPC commissioned Amárach Research to conduct focus groups with consumers who had used PCP finance - the full findings are presented in Annex 1. The issues explored in these focus groups included:

- The PCP selling process from the consumer's perspective
- The level of understanding which consumers have about the PCP product and its various components, i.e. interest rates, monthly repayments, the GMFV, second-hand car values, and refinancing options
- Whether consumers understood the rights and responsibilities of the different parties to the transaction (i.e. car dealers/intermediaries and financial providers)
- An assessment of the extent to which consumers were made aware and understood the terms and conditions relating to servicing, mileage restrictions, small damage and crash repair conditions.

3.5 These findings, which were also explored in a number of in-depth one to one telephone interviews with consumers, are summarised below.

Initial Deposits and Monthly Payments

3.6 While consumers were aware of the initial deposit paid, and whether that was in cash or as part of a trade-in, they did not think of it in terms of a percentage of the overall car value at the time. Most of the consumers who participated in the focus groups said that they could accurately recall their APR and they could compare it to the rates offered for comparable finance products, although it was not possible to test the accuracy of these statements. The consumers asked by the CCPC said that they knew what amount they were paying per month and most based their decision to engage with PCP on the basis of what they could afford each month.

The Underwriting Bank/Finance Company

3.7 Consumers knew that had a contractual agreement with a financial institution for the finance and not with the dealership where the finance was arranged.

Mileage Restrictions

3.8 The research with consumers explored the nature of the information which consumers were given in relation to the specific terms and conditions relating to the PCP contract prior to purchase. The discussions indicated that consumers willingly agreed to a number of standard conditions which were applicable to most of the PCPs.

3.9 When signing up to a PCP, the consumer will agree the maximum number of kilometres they can drive in a year or over the period of the contract. The reasoning for this is to maximise the second-hand value of the car at the end of the contract so that it will help exceed the GMFV and provide consumers with some equity to put towards a new deposit for a new PCP. The discussions in the focus groups revealed that consumers understood the mileage limits and the implications, (in terms of potential charges, of excessive mileage. Many consumers structured their plan around their projected mileage whereby those with higher mileage requirements had their PCPs tailored to suit their needs. The research also found that many dealerships advise consumers to contact them if they think they will exceed their mileage limits as the dealership will renegotiate the mileage limits mid-contract so that consumers can avoid or minimise the charges. Furthermore some consumers 'rolled' their PCP before the end of the term in order to avoid a mileage levy.

Vehicle Servicing

3.10 Another common condition of a PCP is servicing requirements. The dealership can specify where the car has to be serviced, how often it should be serviced and in some instances what the service should include. Although the research indicated that the possible expense of not being able to arrange the service elsewhere could be a source of annoyance for consumers, it also highlighted that consumers were made aware of this condition by the dealers prior to entering the contract.

Wear and Tear

3.11 Penalties for excessive wear and tear are a specific condition of PCP agreements. Discussions with consumers indicated that they were not confident as to the definition of excessive wear and tear and what this could mean at the end of the term. This suggests that this issue may not be adequately explained to consumers at the point of sale including, for example, what the dealership's definition of excessive wear and tear is, how it affects the vehicle's value, and the penalties or charges that may be incurred by the consumer.

Other Fees and Charges

3.12 Additional fees and charges (e.g. documentation fee for setting up the contract, missed repayments fees or repossession charges) are often applied to PCP contracts. It would appear from the research that consumers are adequately advised as to the fees and charges that may be incurred at the beginning and end of the contract.

Perceived Benefits

3.13 While the overall consumer experience of PCPs tended to be very positive there were a number of issues raised that, while perceived by consumers as beneficial, might be evidence of potential risks. These cited benefits of PCPs included:

- **Convenience** - The on-site end-to-end nature of the process was a positive for consumers:

  "I was in at 6pm, approved at 7pm and drove home the next day."

  However, all the information the consumer is presented with in relation to both the new car and the PCP funding it, would raise the question of whether the consumer could fully digest and understand all this information in such a short period of time. In addition, the PRICELab/ESRI behavioural economics experiments on PCP products indicate that the complexity of PCP products has the potential to cause consumers to make incorrect and inconsistent decisions.

- **Approval** - The research revealed that (i) the quick and easy process is regarded as a positive for consumers; and (ii) the majority of consumers were aware of the credit approval process but not everyone believed that they had been checked:

  "It was a very quick and easy process a 'tick the box' exercise -I got a new car, it was like I bought a top in the shop."

  "I am a temp and I wouldn't have got a loan from a bank."

  This raises significant questions as to whether affordability and suitability checks that are in place for other forms of finance are being carried out by the financial institution for PCPs, and the quality of any checks being carried out. As above, most consumers assumed that some form of check had taken place.

- **Misconceptions regarding the equity** – Although the GMFV is set to allow for fluctuations in the second-hand car market, the CCPC's research indicated that consumers could not imagine a situation where there would not be enough equity in the car to roll their PCP. Rather, there is a perception that the providers of PCP finance have 'engineered' the GMFV so that there will always be some equity left in the car in order to encourage consumers to roll into another PCP contract. As discussed in Chapter 2, a sudden decrease in second-hand car values could affect the amount of equity in the car at the end of a PCP contract.

- **Responsible selling** – the general consensus among consumers consulted, which was supported in submissions from and interviews with car dealers, is that when selling new cars, the dealership has a strong incentive to build trust with their customers. This includes providing all the relevant information and advising whether a PCP is the correct product for the individual consumer. For example, PCPs are not ideal for consumers who expect to accumulate high mileage over the period of the contract. This incentive to build trust comes from the need to build a relationship with their customer, so that customers will roll their PCP a number of times with the same dealership, buying a new car from the dealer each time. As noted in Chapter 2, this incentive is not as strong for those dealerships selling second-hand cars.

Issues Reported to the CCPC's Consumer Helpline

3.14 Calls and other correspondence received by the CCPC's consumer helpline were reviewed in order to assess as wide a range of consumer PCP experiences as possible. Table 3.1 displays the number of contacts received by the CCPC's consumer helpline from 2015-2017 concerning PCP.

Table 3.1 Consumer Contacts to the CCPC Helpline, 2015 to 2017[27]

	2015	2016	2017
Number of contacts concerning PCPs	15	29	83

Nine of the contacts received in 2017 complained that the PCP contract was not clearly explained to them. This included the options available at the end of the term, the impact that damage to the car from an accident would have on the agreement or a thorough explanation of the mileage restrictions. A further three consumers complained about pushy sales tactics. Another two had issues with their paperwork, one person said the salesperson was reluctant to give her the full contract and only wanted to provide her with the signature page, and the other said the paperwork didn't match what was verbally agreed. Finally, one consumer said the dealer was not upfront about the price and discounts available.

Some consumers felt it was not made clear to them that there may not be enough equity in the car at the end of the contract period to act as a deposit for the next PCP agreement.

Findings from PRICE Lab

3.15 The CCPC commissioned the Economics and Social Research Institute (ESRI) to undertake a series of behavioural experiments with consumers through its Programme of Research Investigating Consumer Evaluations (PRICE) Lab on the PCP market.

3.16 A summary of the findings[28] from PRICE Lab, which complement the research above, are provided in Box 3.2.

[27] These numbers refer to unique contacts which are individual queries/complaints on a specific issue. The numbers do not include multiple contacts from an individual consumer in relation to the same query/complaint.

[28] https://www.esri.ie/publications/do-consumers-understand-pcp-car-finance-an-experimental-investigation/

Box 3.2 Summary of Results of PRICE Lab Examination of Consumer Behaviour with PCPs

Sample of Consumers

Participants were recruited by a market research company. There were 100 participants, weighted so as to be representative of the population by age (range 22-65), gender and working status.

Research Questions

The study addressed two overarching research questions: (i) How well do consumers understand PCP Finance? (ii) Can understanding be improved by the nature of the explanatory information provided?

Design

Initially, participants were given information about PCP finance deals of the sort commonly distributed by car dealerships. Participants then completed a series of computerised tasks designed to assess PCP comprehension and decision-making. The first was an Adaptive Choice Task (ACT) in which PRICE Lab measured consistency of decision-making over a sequence of similar choices and compared performance for PCP financing with that for HP financing.

The second task required participants to rate a series of PCP finance offers for good value using rating scales. Some deals were objectively superior to others, so this was effectively a test of the likelihood of mistakes. During this stage, the framing of the information presented was varied across participants, some were presented with additional information on the total cost of the PCP deals and some given more in-depth information on the mileage allowance.

The third task was to complete eight Multiple Choice Questions (MCQs) to ascertain explicit comprehension of the main components and relationships of a PCP plan.

Participants were then given one of two intervention documents: the CCPC website advice and a similar sheet developed by PRICE Lab that contained a diagram designed to explain the components of a PCP plan.

The fourth and fifth tasks were to undertake similar MCQs and rating scales to the second and third tasks. Changes in performance on these measures tested improvement in PCP comprehension.

Results

In the ACT, PRICE Lab found that for PCPs participants performed somewhat less consistently than for HPs. In the initial Rating Scales, participants' capacity to identify objectively superior deals was relatively poor. There was no significant impact or improvement when additional cost and mileage information was given to participants.

Similarly poor performance was shown on the initial MCQs. The average consumer correctly answered only 3.49 questions out of 8 – a level of performance only marginally above that which would be achieved by a random selection of answers.

After reading the intervention documents, performance on the rating scales and MCQs improved, especially for those who read the PRICE Lab sheet with the diagram, but also for those who read the existing CCPC information. 67% of participants demonstrated improved comprehension as a result of reading additional explanatory information.

Conclusions
Overall, the experiment provides evidence on both research questions it set out to address: (i) There are substantial shortcomings in consumers' understanding of PCP finance deals; (ii) Comprehension can be improved to some extent by focussed consumer advice.

3.17 The PRICE Lab report goes on to note that even when consumers are presented with all of the most accurate and relevant information and even though they are convinced that the choices they make are the best possible ones for them, consumers are in fact making significant errors of judgement.

> *"Perhaps most striking, however, was performance in multiple choice questions (MCQs) that explicitly tested comprehension. The MCQs did not require any arithmetic, or indeed any kind of explicit calculation, only understanding of the essential elements of ownership, deal structure and directional relationships among key attributes. Yet, following exposure to standard marketing material, performance barely exceeded chance for a group of consumers who were incentivised to provide correct responses and more than half of whom were educated to at least degree level. This amounts to strong support for the hypothesis that consumers struggle to understand the main features of PCP plans. Participants particularly struggled with questions related to the situation at the end of the contract, such as the likelihood of equity and how this relates to the GMFV and movement in the second-hand market."*

4. Current Consumer Protections

Introduction

4.1 The CCPC notes that some traders are describing PCPs as a "Consumer Hire Purchase Agreement". This would suggest that traders understand PCP to possibly be a hybrid of "Consumer-Hire" (rental or lease) and "Hire Purchase" agreements or that it is an arrangement that will not be extended to traders who might wish to hire or purchase a vehicle this way.

4.2 Having considered in detail the relevant legislation it is the CCPC's view that PCP products generally display the characteristics which one would associate with hire purchase. However, unlike a traditional hire purchase, a PCP agreement is typically structured so that the consumer pays a low monthly amount over the contract period plus a final balloon payment at the end if they wish to purchase the vehicle. PCP products are complex and they do not fit neatly into the existing definition of HP and have aspects of a contract for services. These issues are explored further in this Chapter.

4.3 While PCP as a financial accommodation is a relatively recent development, consumers should still be able to avail of a number of existing protections that are available for similar hire arrangements. This Chapter examines those protections and considers whether they are adequate to meet consumers' needs.

The Regulation of Consumer Credit

4.4 Central to any examination of consumer credit regulation is the identification of the type of agreement that comes within the scope of the various provisions that may apply.

4.5 In Ireland there are two significant legal instruments that are concerned with the supply of consumer credit; the CCA 1995 and the European Communities (Consumer Credit Agreements) Regulations 2010[29] (the 'Regulations'). As PCP agreements can be considered as either hiring or leasing agreements where an obligation to purchase the car is not laid down in the agreement, then they are outside the scope of the Regulations. Therefore only the CCA 1995 will be considered further.

4.6 The CCA 1995 was enacted by the then Minister for Enterprise and Employment. The Director of Consumer Affairs was given responsibility for a number of functions in the Act. With the commencement of the Central Bank and Financial Services Authority of Ireland Act 2003, the majority of the Director's functions,

[29] Given effect in Ireland through S.I. No. 281 of 2010

with the exception of some functions including the licensing of Credit Intermediaries, were transferred to the Central Bank.

Advertising of PCPs

4.7 PCPs have been identified by traders as a popular form of car financing. As a consequence, considerable advertising efforts are bringing PCP deals to the direct attention of consumers. This is probably the first indirect engagement that consumers will have with traders offering PCP finance.

4.8 Where such advertising offers to provide credit or offers to arrange the provision of credit, there are a number of information requirements that must accompany such an advertisement. Requiring that a consumer is provided with particular information prior to purchasing a good or service is a common consumer protection measure. In the case of a PCP as a form of financial accommodation, such advertisements will be subject to Part II of the CCA 1995.

4.9 Part II of the CCA 1995 requires that such advertisements must include relevant information such as a statement of the nature of the financial accommodation, the cash price of the car, the APR and the total cost of credit.

4.10 In the event that the PCP market was to develop further and current advertisements were found to be deficient in terms of form or content, then the Central Bank, after consulting with the CCPC and the Minister for Finance, has the power to make amending regulations to address any such issues.

PCP as a General Credit Agreement

4.11 A credit agreement is defined under the CCA 1995 as an agreement under which a creditor grants or promises to grant a consumer a credit in the form of a deferred payment, a cash loan or other similar financial accommodation.

4.12 A PCP agreement, as a financial accommodation that provides for the hire/purchase of the car by allowing a deferred payment, could possibly be considered a credit agreement. Credit agreements are subject to Part III of the CCA 1995. The question then arises as to what type of contract the credit agreement would be provided for? Is it a contract for the sale of the car or a contract of services for the hire of the car?

4.13 Given the considerably larger size of the GMFV when compared to the weekly/monthly instalments, it is likely the case that PCPs will be considered as contracts for services rather than a contract for the supply of goods. This has recently been considered by the European Court of Justice in a preliminary ruling in the case of the Commissioners for Her Majesty's Revenue & Customs V Mercedes-Benz Financial Services UK Ltd (Case C-164/16). The preliminary ruling found that PCP has aspects of both a contract for goods and a contract for services but that a determination would need to be made on a case by case basis, depending on whether there is a realistic prospect that the consumer can avail of the opportunity to become the owner of the goods. As a credit agreement for contracts for services, the content of a PCP agreement would have to comply with the requirements as set out in Section 34 of the CCA 1995.

4.14 Similar to the form and content of advertisements, the Central Bank, after consulting with the CCPC and the Minister for Finance, has the power to make amending regulations with respect to the form or content of credit agreements.

PCP as a Hire Purchase Agreement

4.15 In its presentation, a PCP contract demonstrates many of the features that are commonly associated with Hire Purchase. The PCP contract is entered into between the consumer and the credit institution providing the finance, not between the consumer and the dealership that provides the car to the consumer. As this reflects the intention of both the consumer and provider at the outset and for the reasons set out below, the CCPC's view is that a PCP contract is likely to be considered a form of HP agreement within the meaning of section 2(1) of the CCA 1995. In its operation, however, there may be some differences.

4.16 In support of this view our research shows that some traders describe PCP arrangements as a hire purchase agreement. Where that is the case the agreement will be subject to the provisions contained in Part VI of the CCA 1995 which deals specifically with Hire Purchase. Part VI (i.e. sections 56 to 83) of the CCA 1995 imposes various obligations and grants particular rights to the "hirer" and "owner", the two parties to a HP agreement.

4.17 During the course of a PCP/HP arrangement a consumer is not the legal owner of the car. The consumer will be the "hirer". It is the financial institution which provides the PCP finance that holds the property rights over the asset (the car). The financial institution is the "owner". In PCP contracts, when the GMFV is paid, the "title in" or "property in" the good (i.e. the car) passes to the hirer (the consumer) and if the GMFV is not paid, the title does not pass to the hirer. The PCP always gives the consumer a choice at the end of the term: to return the car or pay the GMFV and thereby acquire "property in" the car, i.e. legal ownership of the car. The consumer is not obliged to buy the car. In the CCPC's view, this means that a PCP is likely to be considered a type of "hire-purchase agreement" for the purposes of the CCA 1995.

4.18 The requirements in relation to HP agreements set out in Part VI of the CCA 1995 include, by way of example, requirements relating to; stating the cash price of the car, the form and contents of the hire-purchase agreement; the hire-purchase price; title in the goods; and implied undertakings as to quality or fitness.

4.19 It is worth noting that the information requirements for HP agreements set out in section 58(2) of the CCA 1995 (e.g. the requirement to state the hire-purchase price, the cash price of the goods to which the agreement relates and the amount of each of the instalments to be paid) may not be adequate in the context of PCP contracts. The section 58(2) requirements are designed to address 'traditional' HP agreements (i.e. traditional instalment-based hire purchase where the final payment is nominal, unlike the GMFV model used in PCP contracts).

4.20 PCP agreements potentially provide four options such as continuing/ renegotiating the hire, returning the car, purchasing the car, or 'rolling' the PCP agreement to apply to a new car. The requirement to state the HP price may be challenging given the mileage limitations and the wear and tear surcharges.

4.21 If a consumer defaults on the payments, the finance provider may have the legal right to repossess the vehicle. However, section 63 of the CCA 1995 allows consumers to end a Hire Purchase agreement and return the car and be liable for 50% of the hire purchase price. This is known as the "half rule" and it limits the liability of consumers to half the HP price of the car. The PCP contract as a HP agreement from the financial institution must therefore indicate the figure for the half rule under the PCP agreement.

The Supervision of PCP/HP Arrangements

4.22 Part VI of the CCA 1995 (i.e. the Part relating to HP agreements) is one of the "designated provisions" in the Act which falls within the remit of the Central Bank. This means that all of the functions granted to the Central Bank under Part 1B of the CCA 1995 apply in respect of Hire Purchase agreements. For example, the Central Bank under section 8H has the power to investigate complaints regarding potential breaches of Part VI, to keep under general review and investigate practices in relation to any of the obligations imposed on persons as set out in Part VI and to publish codes of practice setting out conduct relating to HP agreements. It is also worth noting that the CCA 1995 is a "designated enactment" for the purposes of the Central Bank Act 1942, as amended.

4.23 The Central Bank has adopted a Consumer Protection Code which is designed to ensure a consistent level of protection for consumers. One of the legislative bases pursuant to which the Central Bank issued the Code is identified as section 8H of the CCA 1995. The Central Bank's Consumer Protection Code states that the Code is not applicable to HP agreements or consumer-hire agreements. An addendum to the Consumer Protection Code in May 2008, removed the requirement for regulated financial institutions to adhere to the Code's provisions when "carrying on the business of entering into hire purchase agreements". Therefore, where a consumer sources finance for the purchase of a car though a loan from a bank or credit union, then that would be covered under the Code. On the other hand, where a consumer uses a PCP arranged by a credit intermediary and underwritten by the same bank, this is not covered under the Code.

4.24 Sections 61 and 64(1), respectively, place obligations on the owner (i) to ensure that the contents of any HP agreement comply with required contents provided by the Act and (ii) in certain circumstances, not to enforce any right to recover possession of the good from the hirer otherwise than by legal proceedings. It is an offence for an owner to contravene section 61 or section 64(1) of the CCA 1995s. It is also an offence for a hirer to contravene section 69 of the CCA 1995 which places an obligation on the hirer to give information as to the whereabouts of the goods to the owner.

4.25 In terms of enforcing these requirements, the Central Bank has the power to prosecute offences relating to HP agreements under Part VI of the CCA 1995, which includes the offences referred to above for contravention of sections 61, 64 (1) or 69 of the Act.

4.26 It is worth noting that many of those arranging PCPs are non-bank entities that regardless of their primary business activity, are part of the financial system, yet currently they remain outside the supervisory framework for part of their business. This means that consumers do not have a consistent level of protection when dealing with the same entities for different financial accommodations.

The Role of Credit Intermediaries in PCP Agreements

4.27 While the PCP contract is between the consumer and the finance provider, the consumer's initial dealings will more than likely be with the relevant car dealership. Where the dealer arranges or offers to arrange the PCP finance then they will be considered to be acting as a credit intermediary. This suggests that there are two separate regulatory regimes potentially applicable to arranging a PCP and the content of a PCP agreement:

(i) the provisions relating to hire-purchase agreements as set out in Part VI of the CCA 1995; and,

(ii) the provisions relating to credit intermediaries as set out in Part XI of the CCA 1995.

Credit Intermediaries

4.28 Part XI (i.e. sections 144 to 148) of the CCA 1995 sets out the authorisation regime for, and obligations of, credit intermediaries.

4.29 A "credit intermediary" is defined in section 2(1) of the CCA 1995 as:

"a person, other than a credit institution or a mortgage lender, who in the course of his business arranges or offers to arrange for a consumer the provision of credit or the letting of goods in return for a commission, payment or consideration of any kind from the provider of the credit or the owner, as the case may be."

4.30 The term "owner" is defined in section 2(1) of the CCA 1995 as "the person who lets or has let goods to a hirer under a hire-purchase agreement or a consumer-hire agreement". The CCPC notes that the term "owner" is used in the definition of "credit intermediary" in section 2(1) of the CCA 1995. Construing all of these provisions together, the CCPC considers that, in the context of PCP, the car dealership acts as a "credit intermediary" within the meaning of section 2(1) of the CCA 1995.

4.31 It is worth noting that many of those arranging PCPs are non-bank entities (Credit Intermediaries) who regardless of their primary business activity are part of the financial system, yet currently they remain outside the supervisory framework that regulated entities are subject to.

Supervision of Credit Intermediaries

4.32 In accordance with section 144 of the CCA 1995, the CCPC is the designated authority for authorising credit intermediaries. Section 144 describes the process for applying for and granting authorisation to engage in the business of being a credit intermediary, including the obligations of the CCPC with respect to that process. The remaining sections of Part XI place obligations on credit intermediaries (i) to display a copy of their authorisation,[30] (ii) not to alter the authorisation,[31] and (iii) to explain the nature of the finance arranged to the consumer.[32]

4.33 It is an offence[33] for a credit intermediary to contravene a number of provisions in Part XI of the CCA 1995. Where such offences are committed, the CCPC is the body responsible for prosecuting offences relating to credit intermediaries under Part XI of the CCA 1995 (i.e. breaches of sections 144(1), 144(3), 145 and 148).[34] The Central Bank does not have the power to prosecute credit intermediaries for any of these offences.[35]

4.34 Part XI of the CCA 1995 is one of the "designated provisions" in the CCA 1995 which falls within the remit of the CCPC (and not the Central Bank).[36] This means that all of the functions granted to the CCPC under section 5 of the CCA 1995 apply in respect of credit intermediaries. For example, the CCPC has the power to investigate complaints regarding potential breaches of Part XI, to investigate practices in relation to any of the obligations set out in Part XI and to publish codes of practice.

4.35 It is important to note however that this power to publish codes of practice is limited to *"setting out conduct regarding agreements to which [Part XI applies],*

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[30] Section 145, CCA 1995.
[31] Section 146, CCA 1995.
[32] Section 148, CCA 1995.
[33] Section 12, CCA 1995.
[34] Section 14 of the CCA 1995 provides that an offence under the Act *"for contravening a provision for the purposes of Part IA"* may be prosecuted summarily by the CCPC. Section 4 of the CCA 1995 provides that the provisions of Part XI of the Act are designated as provisions for the purpose of Part IA.
[35] Section 14 of the CCA 1995 provides that an offence under this Act *"for contravening a provision for the purposes of Part IB"* may be prosecuted summarily by the Central Bank. The provisions designated for the purposes of Part IB are set out in section 8G of the CCA 1995 and do not include the provisions of Part XI of the Act.
[36] Section 4(2)(a) of the CCA 1995.

in order to secure transparency and fairness in relation to the terms of those agreements and the conduct of agents dealing with consumers under those contracts".

Box 4.1 Regulation of PCP Car Finance in the UK

In the UK, authorisation from the Financial Conduct Authority (FCA) is required to offer credit to consumers. Consumer credit authorisation is required for a range of activities, including selling goods or services on credit, including hire purchase and PCP (known as Personal Contract Purchase in the UK). The FCA regulates credit intermediaries, which are subject to the FCA's rules, including the FCA Handbook, rules about terms in sales contracts, the Consumer Credit Act and Consumer Protection from Unfair Trading Regulations.

Car finance in the UK has been the fastest expanding consumer credit product which is largely down to a recovery in the car market and the growth of PCPs. According to the Bank of England, gross lending through dealerships for new cars has rapidly increased and the pickup in car finance from dealerships for new cars reflects the increased use of PCP which has been the most popular form of car finance since 2007[37]. PCPs are available for both new and used cars in the UK but are mainly used for new car purchases.

An analysis of new and used car purchases in car dealerships in March 2017 by automotive retail software firm enquiryMAX found that 47.6% of new car buyers and 25.4% of used car buyers opted for PCP finance[38].

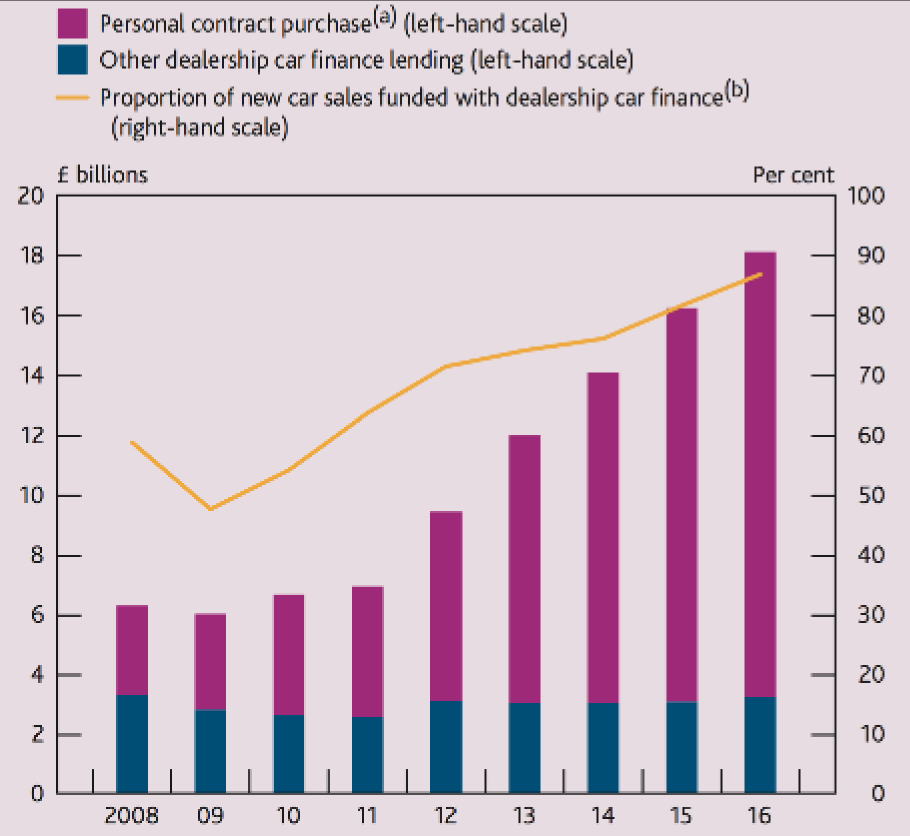
The Bank of England's June 2017 financial stability report noted a surge in consumer credit over the past five years, with car finance making up 29% of the £198bn total. Of the £58bn of car finance, £24bn was held by the banks with the remaining £34bn being held by auto manufacturers and dealers (provided by the subsidiaries of the global car manufacturers). Around 85% of new cars purchased in 2016 used dealership car finance, compared to about half in 2006 and PCP agreements have significantly increased during this period[39] (See Figure 4.1).

Figure 4.1 Value of Annual Dealership Car Finance for new Car Purchases and the Proportion of Private New Car Purchases Funded with Dealership Car Finance

[37] Bank of England (BoE) Credit Conditions Review 2016 Q3 http://www.bankofengland.co.uk/publications/Documents/creditconditionsreview/2016/ccrq316.pdf

[38] PCPs prevalent in March, says enquiryMAX article 18 April 2017 http://www.am-online.com/news/finance/2017/04/18/pcps-prevalent-in-march-says-enquirymax

[39] June 2017 BoE Financial Stability Report http://www.bankofengland.co.uk/publications/Documents/fsr/2017/fsrjun17.pdf



Source:
http://www.bankofengland.co.uk/publications/Documents/fsr/2017/fsrjun17.pdf

Regulatory Environment
The Financial Conduct Authority (FCA) took over responsibility for regulating consumer credit markets in April 2014. The FCA was created by the Financial Services Act 2012 along with the Prudential Regulation Authority (PRA). Whereas the PRA is responsible for regulating firms that could pose a systemic risk to the stability of the financial system such as banks, building societies, credit unions, insurers and major investment firms, the FCA regulates financial service firms and financial markets providing services to consumers.

Earlier in 2017, the FCA confirmed that it was reviewing the motor finance industry because it was *"concerned that there may be a lack of transparency, potential conflicts of interest and irresponsible lending"*. The review will explore the following:

- Are firms taking the right steps to ensure that they lend responsibly, in particular by appropriately assessing whether potential customers can afford the product in question?
- Are there conflicts of interest arising from commission arrangements between lenders and dealers, and if so are these appropriately managed to avoid harm to consumers?
- Is the information provided to potential customers by firms sufficiently clear and transparent, so that they can understand the risks involved and make informed decisions?
- Are firms managing the risk that asset valuations could fall and ensuring that they are adequately pricing risk?

Complaints about PCPs in the UK
The Financial Service Ombudsman in the UK is responsible for dealing with complaints relating to PCPs if the consumer is unable to resolve the complaint with the car dealer or credit provider. The Ombudsman can consider complaints about car dealers as well as those about credit or hire businesses but can only do so in relation to their consumer credit activities. For dealers, this will be for brokering the credit and for the credit provider this will be hire purchase, lending or leasing.[40] The Financial Service Ombudsman revealed complaints related to vehicle finance rose by 64 per cent in 2016 with concerns relating to both hire purchase agreements and personal contract purchase (PCP) deals.[41]

Possible Mechanisms to Enhance Consumer Protection

4.36 By virtue of Part IIIC of the Central Bank Act 1942, it appears that the Central Bank is empowered to use its administrative sanctions procedure as a means of addressing breaches of the CCA 1995 (and breaches of any code of practice adopted by the Central Bank under the CCA 1995), where such breaches are committed by a regulated financial service provider. Among the sanctions that the Central Bank can impose under its administrative sanctions procedure are:

- Caution or reprimand.
- Direction to refund or withhold all or part of money charged or paid, or to be charged or paid, for the provision of a financial service by a regulated financial service provider.
- Direction to pay to the Central Bank a monetary penalty (not exceeding the greater of €10,000,000 or 10% of turnover where the regulated financial service provider is a body corporate or an unincorporated body and not exceeding €1,000,000 where the regulated financial service provider is a natural person and for persons concerned in the management of a regulated financial service provider).

4.37 While it is an offence for a credit intermediary to contravene any of the provisions in Part XI of the CCA, outlined above, the CCPC does not have any comparative administrative sanctions regime similar to that operated by the Central Bank under Part IIIC of the Central Bank Act. Therefore although the CCPC can bring summary prosecutions in respect of particular offences there are no other sanctions available to the CCPC in respect of breaches of Part XI of the CCA committed by credit intermediaries.

4.38 In addition although the CCPC has, in accordance with section 5(1)(f) of the CCA, the power to publish codes of practice in relation to credit intermediary agreements, the CCA does not provide for any sanctions for breaches of such codes of practice.

[40] Ombudsman – complaints about car finance http://www.financial-ombudsman.org.uk/publications/ombudsman-news/79/79-car-finance.htm
[41] Financial Service Ombudsman Annual Review http://www.financial-ombudsman.org.uk/publications/annual-review-2017/pdf/Annualreview-fullreport-AR2016-17.pdf

5. Summary, Conclusions and Recommendations

Introduction

5.1 This section summarises the key findings of this study, makes conclusions based on the evidence gathered and proposes recommendations for consideration by the Department of Finance, the Central Bank and the CCPC.

5.2 The study was conducted in order to compile evidence in relation to:

- the size and characteristics of the PCP market;
- the experience of consumers in the market as well as their ability to understand PCP agreements; and
- the current protections available to consumers under the Consumer Credit Act 1995, as amended.

This evidence is intended to inform any consideration of the market by policymakers and other relevant stakeholders. The study specifically considers the potential for consumer risk and detriment, now and in the future, and proposes a range of potential recommendations, all of which are designed to offer greater protection for consumers when they enter into PCP agreements.

Market Monitoring and Data Collection

Summary

5.3 PCP is a significant part of the car finance market in Ireland. It was introduced on a widespread basis in Ireland towards the end of the last decade, and since then, it has become a well-established method to finance a car. In 2016, between 31% and 34% of new car purchases by consumers were done so using a PCP. In 2017, PCPs were used to finance the purchase of approximately 25,000 new cars, with approximately 33,000 PCP deals entered into by consumers in Ireland in 2015.

5.4 The total value of PCP finance grew by 65% from €488 million in 2015, to €805 million in 2016. The average PCP contract was worth just under €25,000 in 2016, which implies that the average value of a car purchased using PCP was approximately €31,000, assuming a 20% deposit.

5.5 While PCPs were initially created to facilitate the purchase of new cars, the second-hand car market is of growing significant relevance to the PCP market. The proportion of second-hand cars purchased using PCP is increasing, with 12% of PCPs issued in 2016 being for second-hand cars. This was a 100% increase on 2015.

Conclusions

5.6 It is likely given current trends that the number of consumers availing of PCP finance will, in time, surpass the number of consumers using standard HP agreements to finance car purchases.

5.7 Given the substantial increase in second-hand car imports, with a 95% increase from 2015 to 2017, further growth in the second-hand PCP market should be expected. It is noted that the incentive to maximise future sales is not as strong for independent dealers who sell used vehicles, as consumers would be potentially less likely to return to the same dealer to purchase their next car than consumers who purchase from franchise dealers. In the absence of the motivation to increase repeat business, the risk to consumers increases, particularly in the absence of mandated affordability and suitability checks.

In addition, an increased supply of second-hand cars (which happened on a significant level between 2015 and 2017) could reduce the value of second-hand cars generally, thereby impacting on the amount of equity a consumer has in their car at the end of their PCP agreement, with implications for consumers.

Recommendations

Recommendation 1: Monitor development of the sector

As noted in this report, PCPs are a significant part of the car finance market. The CCPC collected data on a voluntary basis for the purposes of this study. Consideration should be given to how this data should be collected on a statutory basis in order to track and monitor the development of the market. There is some volatility evident in the development of the PCP market which would emphasise the need for ongoing monitoring of both the size of the sector in terms of the numbers and values of PCPs underwritten, but also the penetration in the second-hand car market.

Provision of Consumer Information

Summary

5.8 PCPs are clearly attractive to consumers and to traders. They offer consumers the opportunity to drive a brand new car, with a minimal deposit, usually from 10% of the price of the car. As so much of the cost is deferred to the end of the agreement, monthly repayments are lower than with other types of finance.

5.9 The factors driving consumers’ financial decisions in this market, as reported in focus groups, include a significant emphasis on the monthly repayments. Most consumers reported that their decision to buy a car using PCP was based on what they could afford on a monthly basis.

5.10 Research carried out by the CCPC in 2016 supports the fact that consumers focus more on decisions about the car they plan to buy, and less on the method of finance they will use.

5.11 There are also a considerable number of restrictions which apply to these types of contracts. Although the consumers who were involved with this study were generally aware of what these restrictions were, they did not necessarily understand the implications of them. For example, they could not explain what would be construed as excessive wear and tear.

5.12 When compared to other consumer financial products, PCP is particularly complex. This complexity arises not just because of its structure – a deposit, monthly repayments and the GMFV – but because of the numerous calculations and choices that exist for a consumer as they come to the end their PCP. Most consumers chose to roll their PCP and use whatever equity they have in the car as part of the deposit for their next car. But that equity can be affected by the mileage, the condition of the car and future second-hand car values. While consumers can control some of these factors, they cannot control all of them.

In addition, there is a requirement for consumers to consider where their next deposit will come from if they plan to roll their PCP. It is unlikely that they will be in a position to fund the entire deposit from any equity they expect to have in their first car.

5.13 The majority of consumers who enter into PCPs either intend to, or actually roll their agreements, calling into question the extent to which consumers pay the GMFV and become legal owners of the car. This dynamic is important as it creates significant requirements for consumers to both understand and prepare for certain eventualities. For example, if a consumer pays a high deposit at the start of a PCP, this reduces their monthly repayments but has no bearing on the GMFV. At the end of the term, if the consumer decides to roll their PCP, they will use any equity they have in the first car to put towards the deposit for their next car. But as this amount is likely to be smaller than their first cash deposit, they may find that their monthly repayments are far higher on their second car than on their first, an eventuality that may not have been clear to them from the outset.

5.14 As part of this study, a scenario emerged in which some consumers rolled their PCP before the end of the agreement, in order to avoid the impact of the mileage limit. This highlights additional factors of complexity that consumers need to comprehend.

5.15 It emerged in the focus groups that most consumers with PCP had not thought about the volatility in the second-hand car market and most believed that their car's value would exceed the GMFV at the end of the term.

5.16 PRICE Lab findings provide evidence of substantial shortcomings in relation to consumers' understanding of PCPs but that comprehension could be improved through the provision of information.

Conclusions

5.17 The CCPC's consumer research presents differing results in relation to consumers' understanding of PCP products. The self-reported information from the focus groups suggests that consumers are content that they understand the key aspects of the agreements. This is at odds with the information compiled from the CCPC's helpline and the PRICE Lab results. There must therefore be considerable doubt as to the ability of consumers to make informed decisions in this market.

5.18 The fact that consumers spent almost 4.5 times longer selecting the car than the finance points to less attention being paid to the characteristics of their finance decision, with potential risks in terms of suitability and affordability.

5.19 Broadly, consumers know their monthly repayments and understand their contractual responsibilities in relation to maintenance of the car and mileage restrictions. However, they do not fully understand how PCPs work. This conclusion is drawn based on evidence of the product's complexity. In addition, the speed of the approval process means that consumers are required to absorb a considerable amount of complex information in a short space of time.

5.20 PRICE Lab results concerning PCP point to the fact that the provision of more, and better, information can improve consumers' understanding of PCP. However, asking consumers to digest yet more information when buying both a car and finance may be unrealistic, particularly when the CCPC's research highlights that consumers are more focussed on the car than on the method of finance.

Recommendations

Recommendation 2: Ongoing consumer information and education

The evidence collected for this study will further inform the information that the CCPC currently provides to consumers in relation to PCP agreements. As a result the CCPC has begun a full review of its information, taking account in particular of the findings of the consumer research, the PRICE Lab research and more generally how consumers make decisions in this market. The CCPC will complete this review by the end of April 2018.

The CCPC should also continue to conduct public awareness initiatives to highlight key issues, including:

(a) That PCPs may be a cost-effective way of driving a new car, but not necessarily owning a new car

(b) That the GMFV should not be seen as a deposit for a future car

(c) That paying a large deposit on a PCP can have implications for consumers who want to roll their PCP at the end of the agreement, in terms of them having a smaller deposit than for their first PCP, leading to higher monthly repayments

(d) That consumers have the right to terminate a PCP agreement under section 63 of the CCA 1995

Consumer Protection

Summary

5.21 An assessment of the legal framework for PCPs points to some uncertainty. It is the CCPC's view that PCP products generally display the characteristics which one would associate with hire purchase. It is also likely that PCPs will be considered as having characteristics of both a contract for services and a contract for the supply of goods.

5.22 When a consumer arranges a loan through a financial institution, such as a retail bank or credit union, the financial institution must carry out credit and suitability checks in order to comply with the Central Bank's Consumer Protection Code. The Central Bank's Consumer Protection Code requires any regulated entity selling a product to a consumer to ensure that the product meets that consumer's needs and objectives, that the consumer is likely to be able to meet the financial commitment associated with the product on an ongoing basis and is financially able to bear any risks attaching to the product. In the case of credit products, the institution must ensure that a consumer has the ability to repay the debt as required under the agreement, on the basis of the outcome of the assessment of affordability and must ensure that the product or service is consistent with the consumer's attitude to risk.

On the other hand, should a consumer enter into a PCP agreement, which may even be underwritten by the same institution, this is not covered by the provisions of the Code. As a result, a major financial commitment can be entered into without affordability and suitability checks.

5.23 Ireland's regulatory regime for PCPs is different to that of the UK, where PCP agreements are also prevalent and the Financial Conduct Authority regulates credit intermediaries. In Ireland, credit intermediaries require only to be licensed by the CCPC.

5.24 The CCPC's power under section 5 of the CCA 1995 to publish a code of practice is limited and does not mean that the CCPC can establish a regime under its own code of practice which would mirror the effectiveness of that of the Central Bank. Neither the CCA 1995 itself, nor any other legislation of which the CCPC is aware, provides for any sanctions for breaches of a code of practice adopted by the CCPC under section 5(1)(f) of the CCA in respect of credit intermediary arrangements.

By contrast, the Central Bank's administrative sanctions procedure (as set out in Part IIIC of the Central Bank Act) seems to be applicable to both particular breaches of the CCA 1995 and breaches of any code of practice adopted by the Central Bank under the CCA 1995 which are committed by regulated financial service providers.

5.25 Standard hire purchase agreements give important protections to consumers in the form of the third rule and half rule. Although the half rule does limit consumers' liability, with PCPs the contract is structured so that a lot of the cost is deferred to the end. Therefore, it takes longer for repayments on a PCP to reach the point where the half rule will apply, than with hire purchase. In fact, if a consumer pays a small deposit it is likely that s/he will be close to the end of the PCP agreement by the time they reach the point where they have paid half the PCP price.

5.26 Generally consumers are aware that they have two separate agreements, one with the dealer and another with the finance provider. However they do not necessarily think about the fact that the personnel working at the dealership are selling them a complex credit agreement. When asked by the CCPC, dealers generally confirmed that training is in place for the staff who act as credit intermediaries but there does not appear to be independent assessment of the staff and the frequency of training varies.

5.27 At present, car dealerships have an incentive to ensure that consumers have a positive experience with PCPs in order to increase the probability that these PCPs will be rolled by consumers at the end of their contract. This incentive is based on the long-term objective of the dealership to maximise the number of new cars sold in the future as well as at present. If a consumer is sold a PCP which is inappropriate for their needs then it is unlikely they will choose to roll the product at the end of the period.

5.28 Current arrears and default rates on PCP are low. The level of PCP contracts that fell into arrears from 2015-2017 (as of 1st August 2017) was low; 1.4% and the default rate over the same period was 0.3%.

Conclusions

5.29 The absence of mandated suitability and affordability checks creates a potential risk in the PCP market for inappropriate lending by providers and over-indebtedness for consumers. The social costs created by over-indebtedness are well-documented and present a significant risk to the welfare of individual consumers. It is the CCPC's view that regardless of the exact regulatory status of the entity providing the credit, the risk should be assessed in terms of the potential impact on consumers.

5.30 To date, PCPs have worked well for both dealers and their customers, but it is the CCPC's view that aligned incentives are not a sufficient substitute for appropriate regulation in the long-term, particularly given the size of the credit extended to consumers.

For example, in the event of an economic downturn where the demand for new cars decreases, dealership incentives may become more short-term meaning that the alignment in incentives breaks down. In terms of assessing risk, the issue of incentives is also relevant to the spread of PCP agreements into the second-hand car market where the incentives of some traders may be more short-term. Again, future risk should be assessed in this context.

5.31 The focus group research carried out in the course of this study also raised questions as to what affordability and suitability checks are carried out by financial institutions in relation to PCP. While consumers assumed that some form of check had taken place, most were unsure as to what that involved. Understandably, from their perspective, they were most focused on the benefits of the quick approval and speed of the entire process - from application to driving away in a new car. The same factors raise concerns, however, in terms of suitability and affordability and whether checks performed are generic or specifically geared towards the individual consumer.

5.32 It is the CCPC's view that the growth in the market for PCPs should be considered in the context of not just current default and arrears rates but in the context of potential future risk which may arise in the event of either a fall in consumer sentiment and/or a significant fall in car resale values.

Recommendations

A number of options are proposed to enhance the protections afforded to consumers.

Recommendation 3: Review or amend Consumer Credit Act 1995, as amended

The Consumer Credit Act 1995, as amended (CCA 1995), outlines the legislative framework for hire purchase agreements. The view of the CCPC, explained in detail in Chapter 4, is that a PCP is likely to be considered a type of hire purchase agreement. However, the concept of a PCP is not expressly defined in the CCA 1995, as it was not an established form of car finance when the CCA was enacted, or last reviewed in 2003. It would appear, given the significance of the PCP market, that it would be timely for the CCA 1995 to be reviewed to ensure its suitability in relation to this specific, new form of car finance.

Recommendation 4: Update regulatory regime to increase consumer protection

Given the considerable complexity attached to PCP and the regulatory imbalance when compared to other forms of car finance, it is recommended that PCP be brought within the scope of the Central Bank's Consumer Protection Code. This would have the effect of mirroring the protections that are currently afforded to consumers who purchase other types of financial products, including suitability and affordability checks and general requirements around the provision of information[42].

[42] A regulated entity must ensure that all information it provides to a consumer is clear, accurate, up to date, and written in plain English. Key information must be brought to the attention of the consumer. The method of presentation must not disguise, diminish or obscure important information. Source: Central Bank Consumer Protection Code

Section 8H of the CCA is mentioned as one of legal bases upon which the Central Bank issues its Consumer Protection Code. Consideration should be given to how the protections under the Code could be extended to consumers of hire purchase agreements including PCP contracts. Separately the Central Bank has functions for the purpose of the CCA 1995, including "to publish codes of practice setting out conduct relating to agreements which the designated provisions apply, in order to secure transparency and fairness in relation to the terms of those agreements and the conduct of agents dealing with consumers under those contracts". If a revised Consumer Protection Code were adopted, it could include provisions relating to the obligations of those who are engaged in the provision of PCP financing. Any breach of those provisions committed by a regulated financial service provider would be subject to the Central Bank's administrative sanctions procedure as set out in Part IIIC of the Central Bank Act. Otherwise the possibility of the Central Bank issuing a standalone code of practice under the CCA 1995 should be given further consideration.

Recommendation 5: Implement interim arrangement to enhance consumer protection

A transitionary or interim arrangement could be considered where the Central Bank instructs regulated entities underwriting PCPs to only underwrite PCPs where the credit intermediary can demonstrate that it has introduced standardised affordability checks, communicated relevant information in a clear, fair and non-misleading manner and provided a standard information sheet. However, it is acknowledged that such a regime would likely to be a voluntary measure.

Appendices

Appendix 1: Amárach Focus Group Research - Consumer Attitudes to and Experience of Personal Contract Plans – August 2017

amárach research

CCPC

Consumer Attitudes to and Experience of Personal Contract Plans

CCPC | Coimisiún um Iomaíocht agus Cosaint Tomhaltóirí | Competition and Consumer Protection Commission

August 2017/MMCL/SR/S17-222

Background

- Amárach Research was invited by the Competition and Consumer Protection Commission to undertake qualitative research among consumers on the understanding and use of the Personal Contract Plan (PCPs).
- PCPs are a financing tool promoted by car companies to encourage sales of new cars. The car purchase is funded in three distinct phases
  - The Deposit. This can be either cash or a cash equivalent value of a car. Typically this is no more than 30% of the purchase price.
  - The Monthly Repayment. This is a monthly fee paid to the underwriting bank. This is fixed and typically runs for 36 months. This forms about 40% of the purchase price of the car.
  - The Guaranteed Minimum Future Value (GMFV). This is the final balloon payment at the end. It is only at this point that the consumer owns the car outright if all balloon payments have been made. It appears that the car and finance companies' intention is that the value of the car at this point is typically far higher than the GMFV, and that the difference (in effect the residual equity in the car) can provide the deposit for the next PCP programme, there are three options at this point.
- One striking characteristic about the interest rate on PCPs currently is that they are often substantially less than the interest rate charged on other forms of car finance as provided by financial institutions or credit unions. The typical borrowing rate within shares for a credit union loan is c. 5% and even this rate is above any rate that was quoted to us by consumers for their PCP.
- PCPs are different from other forms of car finance in that they are sold 'on-site' by the car dealer.

The Purpose of the Research …

- In essence the research sought to do the following:
  - To find out where and when respondents became aware of the PCP.
  - To gain insight on the PCP buying process.
  - To test the level of understanding that consumers had about the PCP product and its various components – interest rates, monthly repayments, the rights and responsibilities of the different factors in the process (car dealer; bank and consumer) and the GMFV.
  - To test the extent to which consumers had thought through the PCP product and whether it is suitable for them.
  - To assess the extent to which consumers were aware of the behavioural aspects of the PCP – including servicing, mileage, and repair.

Who did we interview…?

- We undertook 6 focus groups over three days. In each focus group there were either 7 or 8 attendees.
- They were recruited at random based on criteria previously agreed with the CCPC.
- They were a mix of ages, gender, social class, car brand purchasers and with different ranges of years driving experience.
- We gave them a pre-task which they completed prior to the group. Each respondent was the key decision maker in undertaking the PCP.
- The Groups were moderated by Michael McLoughlin and Sarah Rooney. Michael McLoughlin is a QFA, while Sarah Rooney is completing her final QFA examinations shortly.
- The Dublin Groups were observed by the CCPC.

LOCATION	DATE	CHARACTERISTIC
Dublin	21st August	First Time PCP
Dublin	21st August	Second Time PCPs
Limerick	22nd August	First Time PCP
Limerick	22nd August	Other forms of Finance
Galway	23rd August	First Time PCP
Galway	23rd August	Other forms of Finance

Prior to PCPs they didn't change cars in a regular pattern …

- Some of this clearly relates to their experience of recession.
- Most PCP owners that we talked to had never had a new car before – we estimate that two-thirds of owners had never owned a new car before their PCP.
- Very few were on a regular car change pattern – many had been driving cars of at least eight years old. Most were changing for a particular reason related to reliability or an impending repair.   Some would not have changed their car at all only for the PCP option.
- They were not brand loyal – they chopped and changed brands at will – in some cases even where they were moving from the first to their second PCP. Where they were more likely to express loyalty was to a particular garage or salesperson. Families appear to have particular garages that they do business with.   Family circumstances, personal experience, getting the best deal and the option of newer makes and models influence the choice of car brand/make/model.

Most have borrowed previously for car purchase…

- They traditionally have used banks and credit unions, and had looked at all these options during their last purchase decision.
- They were all well able to debate the merits of PCPs versus credit union loans or bank loans in terms of rate; monthly repayment and term.
- The key issue for them in considering the finance options is the monthly repayment. They build and structure their purchase decision around this cash flow item. They have a budget figure for car purchase – which is impacted by other commitments.
- This monthly budget figure (or range) drives their purchase decisions

… with the monthly budget defining what they borrow

- The purchasing capacity of their monthly repayment defines what they buy.

- For those who purchase with a PCP the lower APR and the fact that they are only funding 50% of the purchase cost (i.e. excluding the deposit and the balloon payment) over the three years means that they can effectively access a car of double the value that they might otherwise think of – it is this cohort of people who are purchasing a new car for the first time.

- For most the monthly repayment drives what they purchase, rather than the other way round. Those on 0% APRs were particularly wedded to this rate and saw it as a win win (one had intended to buy a new car anyway, but took the PCP in the belief that it made sense to hold onto her own money).

They do understand PCPs…

- Dissemination of information on PCPs comes from two sources:
  - Friends and family - "The lads in work explained it to me beforehand and I didn't give a S*** about what the guy in the garage said to me" - Limerick PCP.
  - Garage Salesmen - Many were unaware of PCPs until they went to a garage. When it was explained to them how PCPs work the possibility of buying a new car came on the radar.

- No-one in the Groups complained about undue pressure to buy a PCP from the salesman, or that it was not explained properly to them. Some felt that the end of contract and rollover into a new contract was more vague in its explanation than other aspects, but no-one came across as not understanding the options or the process.

- They were more concerned with getting a new car with affordable monthly repayments than what was going to happen in three years time – they would worry about that when the time came.

- In our focus groups some of the attendees dealt with the same salesperson end to end – including both car and finance. In other cases there was a specialist finance 'desk' in the car dealership who handled the finance element.

And had considered other options …

- All had considered the previous sources of finance used.
- They were aware of the impact of the product structure and the impact of different interest rates.
- Other factors which supported the PCP purchase included:
  - Convenience. “I was in at 6pm, approved at 7pm and drove home the next day” - Dublin PCP. The on-site end to end nature of the process was a positive.
  - Approval. They were aware of the credit approval process but not everyone believed that they had been checked. “I am a temp and I wouldn’t have got a loan from a bank” - Dublin PCP. Most just assumed some form of check had taken place.
  - Experience of others. “I saw a colleague in work who started with a Golf, went to a Bora and is now on a Passat – and I wondered how it could be done” - Dublin PCP.
  - Lack of paper work. “It was a very quick and easy process a ‘tick the box’ exercise - I got a new car, it was like I bought a top in the shop” – Galway PCP.

The 'Purchasing Power' was the key factor because it enabled them to get a new car …

- They believe that driving a new car creates savings on a monthly basis in terms of repairs, lower fuel consumption and taxation and no need for an NCT. They factor this in when developing their monthly budget.

- The vast majority had never had a new car.
  - "I loved the new car sensation and smell" - Dublin PCP.

- For many purchasing a new car was both prudent, cautious and good sense:
  - "Worry free motoring" - Second time PCPer Dublin.
  - "I was paying huge money on road tax and petrol" [on my old car] - Second time PCPer Dublin.
  - "It runs on the smell of an oily rag" - Second time PCPer Dublin.
  - "It's a great test drive for three years" - Limerick PCP.

They knew the core component elements in detail …

- Repayment Rates.
  - They all knew what they were paying per month. In reality this is the key figure for decision taking.
- APR.
  - Most could estimate to 1 place of decimals. They could compare it to other comparable rates of finance offered for comparable car finances. However monthly repayments were used over APR to determine what they could afford.
- Deposit.
  - They knew the deposit they paid (and whether that was in cash or in kind) although they did not think of it as a percentage of the overall car value at the time.
- The Underwriting Bank.
  - They knew that the agreement was with an underwriting bank – not the garage. Some believed that this made it easier to switch – particularly given the dominance of Bank of Ireland in the marketplace.
- Other fees and charges.
  - They were aware of the fees and charges that were incurred at the start and finish.
- Servicing.
  - They believed that they had to get the car serviced annually by a main franchise dealer. Very few had purchased a service plan. This was the main source of annoyance for PCP holders. It added to the expense as they couldn't do this themselves.
- Mileage
  - They understood the mileage limits and the implication of excessive mileage. They structured their plan around their projected mileage. Some of those on their second or subsequent PCP had 'flipped' their car into a new PCP earlier than anticipated, after 30 months to avoid a mileage levy – with the support and consent of the garage.
  - Those with higher mileage had PCP's tailored to them. The definition of excessive wear and tear and what this could mean at the end of the three years was the only issue people were not as confident on – but it wasn't a worry for them either.

… And could explain the end game in detail

- They knew the concept of the GMFV and their projected final payment. Most respondents were banking on having equity over the GMVF in the car at the end, however some were more dubious about this.

- They knew that they have four options at the end of the PCP:
  - Hand it back (unlikely as some believed they had equity and others saw the whole process would have been for nothing – they would be in a worse off position).
  - Take the equity and use it as a deposit or part deposit on a new car.
  - Borrow the balloon payment and pay it down over two or three years.
  - Use own resources to fund buyout.

- A bit like the PCP they will be influenced in their next purchase decision by the equity in their current car and the monthly repayment. They have not yet decided which of the future options they will take. No-one appeared disenchanted or disillusioned with the PCP concept at this point to the extent that they would rule it out for the future.

- While some are likely to stay with the same brand – they believed that this was a choice that they could reasonably make rather than one that they were forced into. However more believed that they would search and swop around, and decide on their next car at the time. However, the majority of the groups in Galway felt that the PCP tied them into a particular car make.

What remains unclear…

- There are some technical aspects of the PCP that remain unclear to them.
- They have no knowledge of (or bluntly interest in) the business arrangement between the garage and the lender. They assume commission is paid – but “no-one knows” and “it is none of our business” - Second time PCPs Dublin.

… but they know the impact of a crash!

- They are aware that while they do not have full ownership of the car until the final balloon payment, they do have total responsibility if something goes wrong.

- In addition given that for most this is the first time that they have had a new car, they do treat the car with absolute care.
  - "I'd parallel park rather than park beside someone" - Dublin PCP
  - "I am very aware of damage to it – its not actually mine – and I constantly check it for damage" - Dublin PCP.

- Those who were on a second PCP were slightly more sanguine about minor scratches and bumps – and believe more in the goodwill of the garage and the salesman trying to get the next sale as giving them the benefit of the doubt.

- Their attitudes to a crash summed up their understanding of the nature of their nuances of ownership of the car.

- With this in mind they were of the opinion that you cant go around worrying everyday that you will crash or scratch your car. So while it was in the back of their mind they did not let these factors rule their driving experience.

They recognise the reality that they are leasing rather than owning the car

- They understand the difference between outright ownership and what they have. While they used the term ‘my car’, they understood the difference between the ownership status of previous cars and the car purchased under PCP.

- They believed that they were leasing or renting a car for use for three years. They saw car ownership as a constant cost and this method of paying was arguably no different in real terms.

- The PCP owners saw this as comparable to renting a house:
  - “Do you need to own a car?” - Second time PCP Dublin.
  - “I don’t care if I never buy the car” - Second time PCP Dublin.

- Some had experienced minor accidents which had been fixed according to the terms of their contract, but no-one had experienced a catastrophic event such as a write off which could impact.

- The fact that one doesn’t own the car outright from the outset was the key issue for those who opted for other forms of car finance.

What are they concerned about in relation to PCPs…?

- In truth very little. Some are more than half way through their PCP and everything has gone according to plan. For those who have entered a second PCP there were no surprises or shocks during the transition.
- They do worry in an abstract way about a catastrophic event happening to the car, and they are mindful of wear and tear provisions, but not to the extent of changing behaviour.
- No-one appeared to have overstretched themselves financially in monthly budget terms and the PCP did not appear to have created any financial pressure in their lives. Some (a minority) utilise the PCP so as not to use up other borrowing capacity in the credit union or bank.

Things they did not worry about included …

- Most had not thought about of the impact of volatility in second hand car values – which could impact on the residual equity left in the car at the end of the contract period. They believe that the car will be worth more than the GMFV – and to an extent it had been designed and structured to leave some equity if required. Although the Galway group mentioned the impact of a flood of second hand cars in the market in the coming years as PCP’s come to an end.
- They did not feel tied in- The majority did not believe that they would be restricted in switching brands if they decided to enter another PCP.
- They were comfortable with the fact that they had to get the car serviced in a franchised main dealer- They would have been happier to be able to do it themselves but did not see this provision as limiting their choice. They all recognise that they needed to comply with it but viewed it as an additional cost than if they were to do it themselves.
- Timing was not an issue- They were challenged with the fact that they had limited control of the timing of their next car move (i.e. at the end of the contract period) and that that might not suit them if something else was going on in their lives. We used the example of a child starting college. They responded that they were always going to have car costs and that fundamentally they would be able to deal with it at any stage.

… and they all felt comfortable around the T’s & C’s

- Funding the balloon payment- They were keeping their options open – in four of the PCP groups (32 attendees in all), just one or two borrowers were saving for the balloon payment. The remainder believed that they would be able to go again with a new PCP or that they would get additional funding from the underwriting bank to fund the balloon payment over a further 2 years. Some had put no thought into it at all (I will worry about that when the time comes).
- The paperwork- Most had scanned it , but at the stage of signing the smell and prospect of a new car overwhelmed their need to check the contract. A small minority (2 or 3 in total) took the contract home to read before signing it. The Limerick PCP group agreed that they had spent more time on the pre-task for the focus group then on reading the PCP contract before they signed.
- Mis-selling- They did think that everyone had been afforded the opportunity to get as much information as they wanted – and most thought that any gaps in their knowledge could be put down to their lack of interest rather than any slight of hand by the seller. Some believed that they should have looked into it to a greater extent than they did, but in truth most simply scanned the contract before signing it.
- They were all clear on the T’s and C’s -They all felt that the salesperson had gone through the terms in a satisfactory detail and the onus was on themselves if they wanted to find out more.

Those who used other forms of car finance thought differently…

- We had two groups of non PCP purchasers – one in Limerick and one in Galway.

- There were a couple of immediately obvious differences:
  - No-one had purchased a new car.
  - They were much more conscious of mileage and excessive wear and tear.
  - Some were exploring the UK for car purchases and believed that they would make material savings. Going to the UK to purchase a car was a more likely occurrence for this group than taking a PCP.
  - At 0% finance they pondered how many places were making a profit and this made them worry.
  - They all wanted to own the car outright from the start – and this was extremely important to them.
  - They had looked at PCPs – but were left with a sense that they were ‘too good to be true’.
  - They were comfortable in what they know.
  - Their heads had not been ‘turned’ by the prospect of a new car.
  - Many are waiting for more information in the next couple of years to assess its success or failings, they could be persuaded in the future if there is positive press in the coming years.
  - They were more cautious of the two payments at the start and the end.

Their purchase parameters were no different …

- It came down to a monthly budget and repayment schedule.

- They used traditional forms and sources of car finance. Credit unions and bank loans. One had a car financed with the garage.

- They were aware of the opportunity of the PCP but were not persuaded. The barriers to take up were:
  - Absence of ownership. They preferred owning the car outright from the start and the uncertainty over ownership in the future did not appeal to them.
  - "I'd feel like I was driving someone else's car" – Galway PCP.
  - Lack of flexibility. They perceived that there was a lack of flexibility with regard to PCPs. They believed that other forms of finance (e.g. a credit union loan) offered the potential for greater flexibility than the PCP if they ran into economic turbulence. They also felt that the timetable for future decisions was dictated by the timing of the PCP rather than anything else.
  - They were not persuaded by the prospect of a new car. All had purchased a second hand car.
  - Mileage. They did not want any parameters on mileage usage.
  - Service. They were wary of main dealer servicing prices and the lack of control.


IMPLICATIONS AND CONCLUSIONS

PCP purchasers understand the product…

- They are aware of the parameters of the product and understand the product design.
- They are happy with their experience to date:
  - “I have been happy so far – I hope I will be as happy at the end – Galway PCP.
- They understand the deposit, the monthly repayments and the options and choices they have at the end.
- They do not have real concerns despite possible downsides being debated with them.

… but are unaware of market risk

- They view the PCP product as triangulated between themselves, the bank and the car dealer.

- They believe that there is equity built into the car at the end of the PCP, and have not thought about potential changes in the second-hand market or value reduction. They have given no consideration to a scenario where they have no equity in the car.

- They did not for example, consider the impact of car imports from the UK or the decline in the value of sterling, when they were considering the end game for their PCP. Some do believe that there will be a glut of three year old cars coming onto garage forecourts in three years time as people go again.

- They assume that they will be able to refinance the balloon payment at the end if required.

- The only risks that they see are car specific risks:
  - High mileage – which they can control.
  - Car damage through a crash.
  - Lack of repayment flexibility – they cannot repay the loan at any time. Its for three years and this does not change.

- Getting over overexcited – one person warned the group to wait for the car you want and not get sold on what the garage was offering, especially as for many this is the first time they are buying a new car.

They believe that the climate will be benevolent …

- They have an underlying faith in the fact that the car salesperson will want to sell them a new car in three years. That will give them some negotiating power and flexibility in terms of wear and tear, mileage and residual value.

- They do not anticipate any personal budgetary shocks that would require flexibility on the part of the financial provider.

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